THE FREEMAN

IDEAS ON LIBERTY

The Pharmaceutical Industry: Problem or Solution?

Environment and Free Trade

School Violence

The Unseen Costs of Family Leave

FEBRUARY 1994

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Welfare Spending

Before 1962, three out of every four dollars in federal aid to the poor went to them directly, in cash. Today, the numbers are almost reversed. Most federal aid and local welfare spending goes to the "welfare industry" rather than directly to poor people.

In Milwaukee County, Wisconsin, for example, only 37 percent of total welfare spending goes directly to poor people. The rest either ends up in government programs or goes to service providers who are supposed to design programs to help the poor. As a result, antipoverty spending in the county was $1.038 billion in 1988. That was $10,793 for each poor person, or $32,379 for a family of three—well above the poverty line. Yet the poverty rate in the county has not gone down.

—EXECUTIVE ALERT

Private Property

Gain all you can by common sense, by using in your business all the understanding that God has given you. It is amazing to observe how few do this; how men run on in the same dull track with their forefathers. But whatever they do who know not God, this is no rule for you. It is a shame for a Christian not to improve upon them, in whatever he takes in hand. You should be continually learning from the experience of others, or from your own experience, reading and reflection, to do everything you have to do better today than you did yesterday. And see that you practice whatever you learn, that you make the best of all that is in your hand.

—JOHN WESLEY

The Government and Inspiration

In his monograph, "Edison," published by the Newcomen Society in 1948, General David Sarnoff, then president of RCA, said:

The Government is to be congratulated for the encouragement which it is giving to

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the advance of science through the scientific training of young men and women in colleges, universities, and research institutions throughout the country. If out of the thousands of young men and women who are now pursuing scientific studies, there emerges one Edison, then the millions of dollars being devoted to their training will be well worthwhile.

It has been over 40 years since this pronouncement and still no Edison has emerged—at least not from the government-funded universities. It is well known that Edison (February 11, 1847–October 18, 1931) was not happy in school. He was taught at home because the publicly funded teachers found him untrainable.

Edison claimed that genius is 99 percent perspiration. His former employee and lifelong competitor, Nikolai Tesla, said that if Edison were tasked to find a needle in a haystack, he would examine each straw in turn until he found the needle. This can be taught. Meticulous, grinding, repetitive labor is very much a part of most schoolwork. Yet the other one percent, the inspiration, cannot be taught. Without that spark of genius, there is no way to know what a "haystack" is, and why finding a "needle" would be exciting.

Since 1985, I have worked as a community college teacher and a corporate trainer. I can show proof positive that I have helped people learn to use technology. Yet, I cannot imagine any way that any teacher in any school can "train" someone to be an Edison. A million smart young people cannot be collected into a single mastermind. Edison was a once-in-a-century genius who cannot be created by government fiat.

—MICHAEL E. MAROTTA

Benefits of Deregulation

Deregulation of the airline, railroad, and trucking industries in the late 1970s and early 1980s has decreased costs to consumers. And despite claims that more competition would encourage risk-taking, the safety records of all three industries have significantly improved.

Airlines. Since the passage of the Air Cargo Deregulation Act in 1977 and the Airline Deregulation Act of 1978:

- Fares are an estimated 18 percent lower than they would have been under regulation, giving consumers an annual benefit of more than $10 billion.
- Air fares have fallen (in real, inflation-adjusted terms) by more than 20 percent since 1978.
- Accident rates have fallen by 48 percent since 1978.

Railroads. The Staggers Rail Act of 1980 allowed railroads to reduce operating costs and reduce rates to consumers. As a result:

- Shippers save between $3.5 billion and $5 billion a year.
- Railroad accidents have declined 70 percent since the late 1970s.
- Although operating revenues have fallen, expenses have declined even further, making it more profitable for railroads to operate.

Trucking. The Motor Carrier Act of 1980 eliminated the barriers to entry, price discrimination, and price fixing that had characterized the interstate trucking industry since 1935. As a result:

- Between 1980 and 1992, the number of carriers increased from about 18,000 to more than 48,000 and the total number of jobs in the industry increased about 30 percent.
- Savings to the economy are estimated to be $7.8 billion a year.
- The fatal accident rate per 100 million vehicle miles shrank 40 percent between 1978 and 1989.

The trucking industry still is governed by other federal regulations, the elimination of which could save about $28 billion annually on logistical costs. State de-control could bring additional savings of $12 billion per year.

—MELINDA WARREN
"Government Regulation and American Business"

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THE ECONOMIC WAY OF THINKING

PART 5

by Ronald Nash

We are now half-way through our eight part introduction to economics. During the course of this essay and the three to follow, we will examine four important principles of the economic way of thinking.

One of the more valuable things I've learned in life is the importance of viewing economics not so much as a set of doctrines or conclusions, but as a distinctive way of thinking. The principles that underlie the economic way of thinking are not difficult to grasp; they are often matters of common sense. Anyone who is unaware of these principles will not only have difficulty understanding why some things are true in economics, but also why people behave the way they do.

I will introduce the first principle of the economic way of thinking with two accounts of human behavior that don't seem to make much sense, until analyzed in light of our first principle. I will follow my examples with a brief explanation of this principle and then show how understanding that principle can help us understand human action that at first glance appears bizarre or irrational.

Dr. Nash, a contributing editor of The Freeman, *is professor of philosophy at Reformed Theological Seminary in Orlando. His many books include* Poverty and Wealth *(Probe Books) and* Beyond Liberation Theology *(Baker Books).*

How Not to Fly from California to the East Coast

A year ago, a friend and I found ourselves at the John Wayne Airport in Southern California, waiting to board planes that would take us back to our homes on the East Coast. Being a rational person, I of course would be changing planes in Dallas, en route to Orlando. I assumed that my friend would be doing the same. To my great surprise, he told me that he would be making his connecting flight in Minneapolis!

Not wishing to appear impolite I decided not to ask him why he was doing something so irrational. But I hoped my friend would make it since he would find the Minneapolis airport suffering from a mid-winter blizzard.

What Not to Order for Breakfast at Bob Evans

Ordinarily, I enjoy eating breakfast at Bob Evans's restaurants. I usually order fried eggs, over medium, with crisp bacon, wheat toast, and coffee. But on a recent Friday, I entered a Bob Evans and while waiting for the waitress, surveyed the food on the plates at adjoining tables. The lady to my left had a big stack of pancakes plus a side order of

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that great bacon. The fellow behind me had the bacon and eggs. But when the waitress came for my order, I requested a bowl of oatmeal. Not only that, I asked her to hold the brown sugar; I would use artificial sweetener. A bit later, the waitress noticed the tears dropping into the oatmeal and asked if my "breakfast" was all right.

A week later, I walked briskly into the same Bob Evans and without even looking at the menu ordered my bacon, eggs, toast, and coffee. There were no tears that day!

What Was Going on Here?

All of us have seen others behave in ways that seemed irregular, unusual, or even irrational. No doubt, most of us have acted in ways that other people have found peculiar; I know I have.

However, students of the Austrian school of economics know that whenever people are acting, that is, behaving in ways that reflect conscious thinking and choices, their actions are always a function of several factors: (1) the unavoidable fact of scarcity in life; we can never have everything we want. (2) the need to make choices; because we cannot have everything we want, we must choose among available options, and (3) the subjective ranking we place upon the choices open to us. Whenever people act (as opposed to simply responding to stimuli), they are always choosing the option that ranks highest in their personal scale of values at that time.

In cases where it is impossible for someone to have both A and B, a person's choice will reflect the relative value he places upon A and B. People's actions, then, are a reflection of their value scales. Their choices are made in order to help them secure the alternatives that accord more closely with their values.

The value that different people place upon different economic goods (such as having oatmeal for breakfast or changing planes in Minneapolis in the dead of winter) varies from person to person. *I* would never change planes in Minneapolis when flying from Southern California to Orlando. Possibly *you* would never order oatmeal in a Bob Evans restaurant. People's value scales are personal and different. It would be highly unusual ever to find two people who ranked every economic good in precisely the same way.

What's important to understand is that while a person's behavior may appear strange or even irrational to someone else, that action is not irrational to that person. In some way, it makes good sense to one person to change planes in Minneapolis or to have oatmeal one day and then bacon and eggs a few days later.

All of this brings me to the major question of this little essay: *Is there a principle of the economic way of thinking that explains the apparently odd behavior in our two examples?* There is.

The Importance of Incentives

One principle draws attention to the importance of incentives. The greater the benefits people expect to receive from an alternative, the more people are likely to choose that option. The greater the costs expected from an alternative, the fewer people are likely to select it. If we understand what makes human beings tick, we can make general predictions as to how individuals or groups of individuals will respond to changes in their economic situation—in particular, how they will respond to new incentives.

Let's look first at what I regard as my utterly rational selection of oatmeal for breakfast. What I didn't state earlier was the fact that the following Friday I was scheduled for one of an ongoing series of blood tests. About a week before each of these tests, I begin altering my eating habits. Some people might think I'm simply trying to fool my doctor so he won't prescribe new medication or perhaps give me a stern lecture. If that were true, I might well be guilty of being irrational in a different sense of the word. But my action would still be rational in the sense that I was behaving in a way to help achieve an important goal. My action a week later when I ordered my usual bacon

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and eggs reflected the fact that I had had my blood test and could celebrate the good results.

But what about my strange friend who changed planes in Minneapolis? As I pondered his peculiar behavior on my own flight to sunny Dallas, I remembered that he used to live in Minneapolis. Is it possible that he retains some strange obsession with Minneapolis, such that he breaks out in hives unless he visits the place every so often? I ruled that out. Were friends going to meet him for a brief visit at the airport? Since the city was suffering through a blizzard, that seemed unlikely. Then I saw the light!

During all the years he had lived in Minneapolis, the airline he had to fly most often was Northwest. A rational man such as he undoubtedly had a frequent-flyer account with Northwest. The explanation for his apparently bizarre choice was now obvious: He had to change planes in Minneapolis in order to add mileage to his Northwest account. He ranked that high enough in his personal scale of values to incur other costs, such as the possible inconvenience of bad weather in Minneapolis. Incentives matter! If you give people incentives that match their present ranking of values, they will likely select options that reflect those incentives. In my friend's case, he chose Northwest Airlines over American or Delta. In my case, I chose oatmeal over eggs and bacon.

Are the Politicians Listening?

It seems all too apparent that American politicians do not know much about economics. It also seems obvious that they are uninformed about the principles of the economic way of thinking. In this case, they show an obstinate disregard for the importance of incentives when they frame public policy.

When our society establishes programs that provide unemployed people with benefits that approximate or even exceed what they would earn working (after taxes), one can safely predict that many of these people will choose not to work. When a welfare program provides incentives for unmarried women who become pregnant to remain unmarried, we should not be surprised when the illegitimacy rate begins to increase. When minimum wage laws give employers incentives not to hire unskilled employees, we should not be surprised when the rate of unemployment for such workers goes up.

In economics, you get what you pay for. If you give people incentives to do A rather than B, the number of people who choose A—all other things being equal—will increase. Of course, this principle holds lessons for more than just politicians. If we reflect more on what makes us tick, our own actions will become clearer to us. We'll also gain new insight in how to have a more positive influence on the choices made by others. □

The Role of Incentive

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Incentives explain so many of life's events: why higher prices call forth greater supply and why lower prices do not; why racism is tempered in a free market wherein profit-seeking businessmen search for the best labor at the lowest cost; why students work harder in a class where excellence is rewarded and failure is penalized; why capitalist economies do better than socialist economies; why some people quit working and go on welfare; and so forth and so on. . . .

Incentive—nothing less than the interest one has in his own improvement—will mold the future just as surely as it shaped the past.

—LAWRENCE W. REED

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THE PHARMACEUTICAL INDUSTRY: PROBLEM OR SOLUTION?

by Doug Bandow

In his State of the Union speech President Bill Clinton warned that his entire economic program could fail if Congress did not approve serious health-care reform. Alas, his economic program could also fail if Congress approves the wrong sort of health-care reform. The result could be a simultaneous medical failure and fiscal disaster.

Unfortunately, the administration is moving in the wrong direction with a tax- and regulation-heavy reform proposal. One of the reasons that it is more likely to hurt than help is the fact that its proponents seem as interested in punishing supposed villains as in improving the lives of patients. Doctors and insurance companies have long been popular targets of populist wrath; so, too, have been pharmaceutical companies. For instance, during the 1992 presidential campaign President Clinton promised to "stop drug price gouging." His wife's task force had little more regard for the drugmakers, complaining of their "sins of the past," including charging thousands of dollars a year for some drug therapies. Worried one industry lobbyist, "administration officials have made a political calculation that they need to go to war with us."

Task-force members responded to analysts who spoke of market-oriented health-care reforms by arguing that the marketplace would not limit prices "of single-source drugs for which there is no therapeutic equivalent," as if the purpose of patents was something other than allowing inventors to earn a generous reward for their labors. But the President apparently shied away from formal price controls because of opposition from even liberal Democratic legislators. Still, his program would hit the industry with measures very much like price controls: Medicare would demand a 17 percent (up from 15 percent in the initial draft) rebate on prescribed drugs, the Secretary of Health and Human Services could further bargain down prices and refuse to allow the purchase of drugs deemed to be overpriced, an "Advisory Committee on Breakthrough Drugs" would collect confidential industry information and assess the "reasonableness" of drug prices, and the overall health-care plan would press people into managed-care insurance plans that would limit access to pharmaceuticals.

Congressmen, too, have been pressing for controls over prescriptions and prices. For

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instance, Senator David Pryor (D-Ark.), chairman of the Special Committee on Aging and a close friend of President Clinton, has long used his committee to demand limits on pharmaceutical prices. He testified before the President's Task Force on Health Care Reform, complaining that "manufacturers can essentially set the launch price, without the health care system having any idea of whether the price is 'fair' or even 'reasonable'." Yes, continued research and development is important, he acknowledged, but "that does not mean—as a matter of public policy—that the manufacturer should be able to charge whatever the market will bear." Indeed, he argues, the companies will gain an unwarranted windfall from the Clinton program's inclusion of pharmaceuticals, which, in his view, alone warrants regulating the industry.

Other Congressional critics of the drug industry include Representatives Sonny Montgomery (D-Miss.) and Pete Stark (D-Cal.), and Senators Byron Dorgan (D-N.D.) and Edward Kennedy (D-Mass.). For instance, Representative Montgomery has proposed limiting the prices of drugs purchased by Veterans hospitals. Representative Stark, supported by the American Association of Retired Persons, has suggested creating a U.S. equivalent of the Canadian Patented Medicine Prices Review Board to slow drug price increases. Senator Dorgan wants to cut pharmaceutical tax credits and create a Prescription Drug Policy Review Commission. Senator Kennedy hopes to force drugmakers to provide their products for lower prices to entities funded under the Public Health Service Act.

Even some doctors contend that pharmaceutical prices are too high. Columbia University's Paul Meier, a consultant to the Food and Drug Administration, says that "There's a limit to how much we should play the market." As he explains, "If someone who finds a pill that would save babies from some dreadful fate says, 'I'm charging an outrageous amount but it's worth it,' I would say that's morally corrupt." How to set a "fair" price? Dr. Peter Arno of New York City's Montefiore Medical Center proposes establishing prices based on those of comparable products or drugs in other nations.

In short, the average American could be forgiven for thinking that the drugmakers deserve to be damned. Yet all the attention being given to pharmaceuticals seems odd, given their relatively small role in the health-care crisis. Prescription drugs account for roughly eight percent of total health-care expenditures, half that of three decades ago and *far lower than in most European countries*. The average consumer doesn't know that, however, because the government covers a smaller share of drug costs in America, meaning that consumers pay more of the expense directly and therefore complain more vociferously to their elected officials. In fact, this goes a long way to explaining why President Clinton and many Congressmen are so busy attempting to develop well-publicized "solutions" to the nonproblems in this area.

A Successful Industry

Before the government "reforms" pharmaceuticals, it needs to recognize that drugmakers constitute one of America's most successful economic industries: U.S. firms developed roughly half of the drugs marketed worldwide during the 1970s and 1980s. According to the General Accounting Office, pharmaceutical companies are only one of the 11 high-tech industries that it studied which did not lose ground internationally during the 1980s, but rather "maintained their strong position over the decade." Between 1973 and 1986, American firms accounted for ten times as many drug patents as Germany and Japan, 16 times as many as Great Britain, and 20 times as many as France. Research and development spending has grown fifteen-fold from 1970, to more than $9 billion. R & D also rose significantly as a percentage of revenues during the 1980s—at a time when companies are being accused of price-gouging.

Moreover, while drugs may be expensive, the lack of drugs is also expensive. That is, drugs often replace higher-priced medical

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operations and treatments. Actigall dissolves gallstones, for instance, and thereby saves an estimated $2 billion annually precisely *because* 350,000 patients use it. Surgery for ulcers usually runs more than $25,000, while taking medication may run just $1,000 annually; the resulting savings totals at least $3 billion, even more including the economic gain of workers not incapacitated by surgery. Medicine for arthritis and osteoporosis permits some elderly patients to avoid institutionalization. Patients who spend $300 a year on drugs to treat angina can thereby avoid coronary bypass surgery running $40,000 or $50,000. The beta-blocker Timolol reduces the number of second heart attacks by 16 percent and saves about $2 billion every year. The Battelle Institute estimates that for just eight leading diseases between 1968 and 1989 drugs saved 671,000 lives and $83.8 billion.

Thus, a drug's price tells us nothing about its value. Explains Dr. Herbert Gladen at the Baltimore VA Medical Center, "higher-priced drugs may actually be more cost-effective if they have greater efficacy, wider therapeutic range and are less costly to prepare and administer." Indeed, because even expensive prescription drugs are so cost-effective, limitations on their use actually increase total medical expenses. A 1988 Louisiana State University study, for instance, warned that if Medicaid, the joint federal-state program for lower-income people, restricted drug coverage, overall costs were likely to rise between 4.1 and 15.5 percent. Just such an attempt by New Hampshire to limit the number of prescriptions for Medicaid recipients caused an upsurge in doctors' visits, hospitalizations, and nursing home admissions. The legislature dropped the ill-considered regulations within a year.

Are Drug Prices too High?

Are drug prices nevertheless too high? Senator Pryor, for instance, complains that pharmaceutical prices rose far more swiftly than the general inflation rate during the 1980s. Drug prices are higher here than in other nations, he contends, and new drugs are extraordinarily expensive. "While these new drugs helped to reduce hospital stays, and in many cases avoided more costly medical interventions," he acknowledges, "there was no indication that the prices for these drugs had any relationship to their costs of production and development, or were priced reasonably."

However, one should always be skeptical of the partisan use of statistics, since, when tortured, they will confess to anything. Warns Robert Goldberg of the Gordon Public Policy Center, the Bureau of Labor Statistics has failed to incorporate such changes as the greater availability of generics into its figures, meaning that the reported drug-price index may be inflated by as much as 50 percent. In any case, for most of the 1960s and 1970s drug-price increases remained *below* the overall inflation rate, as well as the cost of medical care. As inflation waned in the 1980s drug prices followed the overall trends but fell less quickly.

Moreover, by the mid-1980s generic substitutes for brand-name drugs were entering the market more quickly as a result of legislation passed in 1984 speeding the FDA approval process. While this step reduced the cost of older medications, it had the opposite effect on new releases. Firms found the effective life span of their brand-name products to be shorter, forcing them to focus more on the introduction of new products, which typically cost the most, and *charge more when the drug was released in order to recoup development costs.*

Moreover, the price hikes of the 1980s are not carrying over into the 1990s as competition has intensified. "The market for drugs has changed dramatically since 1981, particularly in the last three years," reports Robert Goldberg. According to the Boston Consulting Group, industry-wide average discounts had quadrupled to 16 percent in 1992 over 1987. New drug prices in 1991 and 1992 were 14 percent lower than comparable products in the past. Some of the cuts were drastic—36 percent for new heart drugs, for instance. HMOs, hospitals, and drug mail-order firms were also gaining an increasing

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share of drug sales and simultaneously winning discounts of up to 30 percent from list prices. And the pressure for price-cutting will increase as larger number of drugs lose their patent protection. Observes Dr. Goldberg, "by 2000, 200 drugs with $22 billion in sales will be off patent."

In any case, politicians today are likely to do no better than those who tried over the past several thousand years to set "reasonable" prices for any number of goods and services. Prices respond to supply and demand, not moral fervor. There is no objective standard by which Senator Pryor or anyone else can call one price reasonable and another unreasonable. Nor is there anything about the market that gives participants the power to "price-gouge."

After all, the market is competitive—there are some 22 major drug firms, and no company has more than a 7.2 percent share. (The industry was even more fragmented in 1962, before more stringent federal regulatory standards, passed in the aftermath of thalidomide-induced birth defects, drove smaller companies out of business. The new FDA "regulations created pronounced economies of scale for drug innovation, which steadily increased over time," reports author Terree Wasley.) The only way a firm can gain "monopoly" power is by developing a good product protected by a patent. Patents, however, are required to induce firms to spend money on research and development. After all, the average cost of developing a drug runs $359 million, according to the Office of Technology Assessment (OTA).

High Costs of Federal Approval

Much of this expense is due to the federal drug approval process. Companies must convince the FDA that prospective products are not only safe but effective; separate applications, which typically run 100,000 pages long, are required for different treatments by the same drug. Since 1962 both the total cost of bringing drugs to market, and the length of time devoted to testing and review, effectively cutting a product's patent protection, have more than doubled. In 1984 Congress passed a measure extending drug patent lives, but that step only ameliorated, rather than solved, the problem.

The costs of a process that averages 12 years would be high enough for any industry. But, notes Michael Ward, staff economist at the Federal Trade Commission, "the very nature of the lengthy drug development process makes the pharmaceutical industry susceptible to harm from unnecessarily stringent regulations."

Most importantly, the risks involved are enormous. Pharmaceutical companies find many more dry holes than gushers: 70 percent of new drugs *that reach the market* are estimated to lose money. Most never get beyond the research stage. There are typically 30,000 to 45,000 medical articles on drug therapies a year. Government patent grants for drugs usually range between 2,000 and 4,200 a year; companies list about half that number as investigational new drugs with the FDA. Another half fall out by Phase Three of the testing process and companies end up filing applications for barely 80 to 250. The FDA then approves between 20 and 60. Concludes Ward, "In all, firms will market about one out of a hundred of the products for which they have developed patents."

Studies suggest that the 1962 amendments have had little impact on the introduction of ineffective drugs—companies don't like duds because they don't make money if their products don't work—but have reduced the rate of introduction of new drugs by two-thirds and the speed with which they enter the market by one-half. The United States has also lost some of its edge over other industrialized states, which permit the sale of safe and effective drugs still prohibited by Washington. Because patients suffer when they receive no medicine as well as when they receive bad medicine, on net the tightened federal controls have made more Americans sicker and allowed others to die.

Even so, some critics argue that the drug companies are making too much money. A

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COURTESY SCHERING-PLOUGH CORPORATION

widely cited OTA study contended that "returns to the pharmaceutical industry as a whole over the 12-year period from 1976 to 1987 were higher by 2 to 3 percentage points per year than returns to nonpharmaceutical firms, after adjusting for differences in risk." Average industry profits ranged between 13 and 14 percent during the 1980s.

This rate of return hardly seems unreasonable given the very high risks of both failure and regulation, which Robert Goldberg believes the OTA has underestimated. In any case, this level of return is probably not sustainable, given the increasing competition within the industry and cost consciousness of consumers. In particular, OTA's future estimates overlook how dramatically generic products have been eroding brand-name drug prices over the last decade.

Moreover, Dr. Steve Wiggins, an economics professor at Texas A & M University, suggests that "a common misstep by industry critics is to rely on accounting data to measure industry returns" when such figures are "unreliable because accounting conventions require the expensing of research and development." Wiggins contends that compared to the cost of capital, drug company returns look far from impressive. He compares the industry's capital costs, which ran from 15.1 to 17.2 percent between 1980 to 1990, with an estimated return of between 13.5 and 16 percent, which, he says, indicates "competitive returns."

Research and Development

It is also important to recognize that the industry's profits were largely channeled into research. Last year the drugmakers spent more on R & D, $12.6 billion, than they earned in profit, $10 billion. Industry R & D grew by a 15 percent compound annual rate in the 1980s. As a percentage of

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sales industry, R & D approaches 17 percent, nearly twice that for the rest of the health-care industry and treble that for the electronics industry. Even the OTA acknowledged that its "findings on returns to pharmaceutical R & D and to the industry as a whole explain why R & D expenditures have risen so fast throughout the 1980s. Investors followed the promise of high returns on future innovations." But ignored by the OTA is the fact that a lot of this money, as much as one-third, according to Dr. Goldberg, is going into biotechnology, which is riskier than traditional drug research.

What does all this money produce? The Boston Consulting Group points to a score of new drugs expected to be approved later this decade to combat AIDS, allergies, Alzheimer's, asthma, arthritis, cancer, depression, diabetes, glaucoma, herpes, hypertension, obesity, strokes, and many more diseases. With these conditions costing untold lives and an estimated $400 billion a year, it seems foolish to begrudge the pharmaceutical industry a healthy return on its investment. Critics should be celebrating the industry's success rather than carping about an allegedly "excessive" percentage or two of profits.

Unfortunately, new federal restrictions would simultaneously raise the industry's cost of capital and reduce its rate of return, forcing firms both to cut R & D and distort their research efforts. Companies would skew their efforts to products that would more easily win regulators' approval for price increases and also shift money to unregulated investments, *such as marketing*, that would involve less risk and a better return.

The form of price controls wouldn't matter. All would hurt patients—not by denying them access to current therapies, since those drugs are already on the market, but by discouraging new treatments from appearing. The cost to patients of losing new medicines could be staggering. Between 1975 and 1989 American firms developed half of the 66 top drugs introduced in the marketplace. French enterprises, in contrast, created just three. The most important difference between the two nations is government policy. Observes P.E. Barral, "In France, the calibre of pharmaceutical research is seen as having deteriorated, because severe price control has encouraged French companies to give priority to small therapeutic improvements which are useful in price negotiations. Such systems tend to stifle originality and induce risk aversion." At the same time, drugs accounted for 16.7 percent of French health expenditures, twice America's level. Moreover, per capita spending on drugs is almost three times as high in France.

Health-care reform should involve a search for answers, not villains. In the case of pharmaceuticals, the system is working: A highly competitive industry is leading the world in the discovery and marketing of new treatments and cures. Although drugmakers have an incentive to invest heavily in R & D, pharmaceuticals account for a lower proportion of total medical expenditures than in socialized systems, while at the same time helping to hold down overall medical expenses. If the administration and Congress nevertheless put ideology before prudence and tighten controls over the drug industry, they risk killing the golden goose that has provided so many benefits for so many patients. □

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THE FREEMAN
IDEAS ON LIBERTY

ENVIRONMENT AND FREE TRADE

by Jo Kwong

Environmental activists, who typically take a unified stance on major issues ranging from global warming to endangered species protection, experienced an unusual split with regard to the North American Free Trade Agreement (NAFTA). Generally speaking, environmentalists divided between those who were convinced that free trade would lead to greater damage to the environment, and those who believed that freer trade would stimulate national economies, ultimately creating more resources to help protect the environment.

NAFTA brought these two positions into stark conflict. Most vocal was the anti-NAFTA environmental lobby. The Sierra Club, Friends of the Earth, and Public Citizen, among others, argued that NAFTA would provide an opportunity for U.S. companies to migrate to Mexico and escape more rigid American environmental laws. Larry Williams, international program director for the Sierra Club, cautioned that the flight of factories from the United States to Mexico: "would increase pollution loading levels on the continent and would trigger pressures within the United States to lower environmental standards to improve competitiveness in order to stop the flights."[1]

This thinking, however, is flawed on several counts. First, there is little historical evidence of polluting industries migrating to countries where environmental standards are lax. While many developing countries are experiencing rapid industrial growth, this reflects the economic stage that they are going through, rather than environmentally induced migration. Polluting industries which spend heavily on controls remain concentrated in the developed countries. Ironically, it was the closed, protectionist countries—particularly in the former Communist world—that became pollution havens.

Environmental regulations pose a negligible factor on migration decisions because they typically comprise less than 4 to 5 percent of total costs. Other factors may easily overwhelm such a modest cost savings: On my last trip to Mexico City, several people indicated that problems like unstable telephone service are of far greater concern than environmental considerations in making location decisions.

Moreover, irrespective of the level of regulation, companies are fearful of liability arising from environmental accidents. A firm's desire to protect its reputation in its home market weakens the temptation to cut environmental costs—companies are sensitive to the demands of "green" consumers in export markets.

Another common environmentalist objection to reducing trade barriers is that doing so will inhibit harmonization of environmental, health, and safety standards regarding production processes. For example, in a highly publicized case involving yellowfin

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tuna imports, environmental activists ran newspaper advertisements with the headline "SABOTAGE! of America's Health, Food Safety and Environmental Laws." The ads argued that "the only thing free about free trade is the freedom it gives the world's largest corporations to circumvent democracy and kill those 'pesky' laws that protect people and the planet." The activists were furious about a GATT ruling against a U.S. ban on tuna imports from Mexico, imposed because the United States alleged that Mexican fishing boats kill too many dolphins. Yet, according to the *Journal of Commerce*, the U.S. killing rate was significantly greater than that of Mexico: "In 1988 the US fleet caught 70,000 tons of yellowfin tuna and killed 19,000 dolphins; in 1990 the Mexican fleet caught 120,000 tons of yellowfin tuna and killed only 16,000 dolphins."[2] Thus, this controversy provides a better example of economic protectionism than environmental destruction.

Other allegations by the U.S. environmental lobby illustrate how politics has overtaken science in the making of domestic law. Activists warn, for example, that foreign nations might use pesticides that are banned in the United States. Therefore, trade restrictions are necessary. However, the United States greatly overregulates most pesticides: many are banned even if the residues found in food are minuscule and threat to human health is virtually nonexistent. Much of this is a result of the Delaney Clause, a provision of federal food safety law, which states that "no additive shall be deemed to be safe if it is found to induce cancer when ingested by man or animal." Much has changed since the clause was added in 1958, particularly the ability to detect minute chemical residues measured in parts per million, even parts per billion. Thus, the law now bans all sorts of products that would have been considered perfectly safe in 1958.

Such draconian rules are inefficient in America; in poorer, Third World nations they could prove to be downright fatal. DDT is a case in point. U.S. environmental activists, not satisfied with banning the substance in America, are still trying to ban it elsewhere around the world. To this day, serious controversy persists about whether DDT really poses a serious environmental danger. The World Health Organization, the U.S. Surgeon General, and the National Science Foundation have been unable to document many of the charges raised against DDT over the decades.

In contrast, the harm to human health from the ban on DDT has been very real. In just two decades of DDT use, malaria deaths in India were cut by 98 percent, raising the average life span by 18 years. In the nearly 20 years since the ban, malaria death rates have soared. Similar trends have been observed in Sri Lanka, Bangladesh, Burma, and Thailand. Thus, the environmental benefits of the DDT ban may have been far outweighed by the human costs.[3]

As this case suggests, many environmentalist arguments against trade reflect more emotion than rational analysis. In fact, with freer trade it is probable that Mexican ecological, health, and safety standards would evolve towards U.S. standards, rather than vice versa. One reason is that most international companies have universal policies in place regardless of where they are operating. They don't set lower standards for operations in less developed countries. In this way Mexico's environment would be enhanced by opening up trade.

Furthermore, companies typically expect rising environmental standards in developing-country markets, so they tend to introduce state of the art technology initially. One GATT report published early last year cited cases in which firms gain a competitive edge by investing first in clean technologies.

A Conflict of Visions

If the environmental arguments against freer trade are so flawed, why are they nevertheless held so tenaciously? One reason is the intellectual framework of many environmental activists. Broadening trade runs against the environmental vision, particularly that of local self-reliance and a return to a simpler, low-technology world.

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Consider the argument of David Morris of the Institute for Local Self-Reliance: "Most people believe that a global economy is the only path to a higher standard of living as well as the inevitable next step in economic evolution. The economic emphasis on imports and exports continues to guide our thinking even when we can see that it endangers the survival of humans and other species."

In his view, the "key to achieving a Green future . . . is localizing the world economy."[4] The problem with this quaint way of thinking is that it ignores elementary economic concepts. For instance, as long as trade is voluntary, both partners benefit; otherwise they wouldn't trade. The buyer of a shirt, for example, values the shirt more than the money spent, while the seller values the money more. Trade makes the world economy more efficient by allowing nations to capitalize on their strengths.

Of course, Morris accepts trade within his local region, but where does he draw his trade boundary lines? If it makes sense for Morris's butcher and baker to trade in their region, how about trading with the community next door? Morris's vision makes no rational sense, but retains enormous emotional appeal.

Another point that should interest environmentalists is the fact that opening economies to the competitive global marketplace forces nations to become more efficient and waste fewer resources. For instance, in the Soviet Union every barrel of crude oil consumed produces $253 of GNP; the corresponding outputs for the United States, western Germany, and Japan are $341, $420, and $639, respectively. Similarly, Swedish sawmills use 98 percent of a tree in timber production whereas Malaysian mills use only 40 percent. The sort of waste and inefficiency evident in more closed economies is responsible for much of the environmental degradation of the world today. Competition, which forces technological improvements and the modernization of plants and equipment, can vastly enhance environmental quality.

Freer trade would boost environmental amenities in other ways. For instance, much of the current pollution on the U.S. side of the border results from crowding on the other side, largely as a result of the *maquiladora* program. That program gives special tariff treatment to Mexican industries that import U.S. products for assembly and re-export. It originally required Mexican firms to locate along the border in order to receive the program's benefits. While these restrictions have been eased, others remain which encourage firms to remain in the border area. Free trade would reduce today's artificial incentive for border crowding.

The bulk of the environmental improvements are most likely to occur in Mexico. Companies operating in developing countries bring new technologies to market and, for reasons mentioned earlier, are likely to adhere to American standards. In addition, Mexican companies would find they have to adhere to standards acceptable to U.S. consumers in order to successfully export. Just the promise of free trade is already encouraging U.S.-Mexico cooperation on the cleanup of their common boundary. Before NAFTA, U.S. activists largely ignored environmental problems in Mexico. Now, the two countries are hammering out details on the Border Plan, the most comprehensive attempt to cooperate on cleanup.

Perhaps the biggest reason for environmental gains in Mexico from freer trade, however, would result from increased economic prosperity. To some environmentalists, this seems backwards. Many argue against trade because it encourages industrialization, which in turn, is blamed for pollution. Yet the experience of Western developed countries is just the opposite. Over the long term, emissions eventually fall, even as economic growth continues to increase. Several years ago, Hoover research fellow Mikhail Bernstam detailed what he calls "the environmental split of the 1970s and 1980s"—a divergence between consumption and pollution involving Western market economies and the socialist world. He found that resource use and discharges began to decline rapidly in those nations with competitive markets, even as eco-

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nomic growth continued. In contrast, during the same two decades, consumption and environmental disruption were rapidly increasing in the USSR and European socialist countries even though their economies slowed down and eventually stagnated.[5]

Bernstam's conclusions are borne out by other studies as well. Gene Grossman and Ann Krueger examined air quality in urban areas of the developed and developing world. Their analysis related the level of pollutants to the level of the nation's per capita GDP. They found that concentrations of sulfur dioxide have risen with incomes at low levels of per capita income; fallen at higher levels of per capita income; and leveled off when per capita income reached about $5,000 (1988 U.S. dollars).

The basic point is that countries must be rich before they can be clean. As societies become wealthier, they attach a greater value to environmental quality. Ecological prosperity is a luxury that only developed nations can afford. Trade enables countries to become richer, and, as the studies suggest, this in turn reduces pollution.

Free Market Environmentalism

Another interesting finding of the Bernstam study was that the strictness of government environmental regulation does not correlate with the drop in pollution. If anything, he writes, there is a slight *negative* correlation. Far more important in determining emission levels is an economy's incentive structure. Thus, as we discuss markets and trade within North America, we should consider using markets in natural resources to foster incentives for environmental stewardship.

Free market environmentalism is premised on the idea that the failure to apply markets has led to many of today's environmental problems. Air, water, and land pollution are often the worst on common property resources such as those owned by the government. In these cases, no one is responsible for seeing that resources are used efficiently and adequately protected.

This is the essence of the standard textbook concept called the "tragedy of the commons," whereby users of communal land will use the property as intensively as possible, since they gain little benefit from conserving the resource. Users of communal grazing lands face the incentive to boost personal gains by overgrazing the land at public expense. In contrast, users of private land face the incentive to consider the costs of maintaining the pasture at varying intensities of grazing. Of course, many people object that the owners will exploit the land for profit, caring little about environmental preservation. However, property rights give even an uncaring owner a financial incentive to preserve his land, since overgrazing will lead to both economic ruin and environmental devastation. By maintaining the property, he maximizes both.

Unfortunately, the standard approach to environmental problems in the United States has been regulatory rather than market oriented. But most major environmental initiatives, such as Superfund, the Endangered Species Act, and the Federal Water Pollution Control Act, have fallen far short of their goals. Most have been extremely expensive and relatively ineffective. Some have even created severe disincentives for people to preserve the environment. Consider the Endangered Species Act, intended to protect plants and animals that are experiencing serious population declines. Under the Act, it is a federal crime to use land in a way that endangers the habitat of protected plants and animals. Once an endangered species shows up on private property, the landowner is no longer free to use the land without federal approval. Some owners have lost millions of dollars after the discovery of protected wildlife on their property. As a result, many now discourage natural habitat and destroy any protected species that they find—the "shoot, shovel, and shut-up" strategy.

Such problems are no stranger to Mexico. As Roberto Salinas, Executive Director of the Centro de Investigaciounes Sobre la Libre Empresa in Mexico City, writes, "the lack of property titles in rural farming areas

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has forced peasants to turn to burning the rich forests in southern Mexico in search of new arable land." As Mexico confronts its many environmental problems, hopefully its leaders will consider more efficient market-oriented conservation strategies. They are more likely to do so as part of a freer economic and trade regime.

Summary

In the end, anti-free trade environmentalists need to address the evidence and, equally important, rethink their warped vision of the future, a "shallow ecology" that, intentionally or not, aims at protecting the health and affluence of people in the developed countries. Argues Roberto Sanchez, an environmental specialist at the Colegio de la Frontera Norte, a research institute in Tijuana, environmental changes will only occur "if the American environmentalists give up some of their romantic notions and let [Mexico] find its own way." Environmentalists may "want to save the planet, but it is not the same planet on their side of the border as it is on [Mexico's]. They can afford to defend the environment for its own sake. Our people must use the environment to survive."[6]

Trade negotiations, including but not limited to NAFTA, present unique opportunities to coordinate trade with environmental policy. The evidence is overwhelming that opening markets will provide both economic and environmental prosperity for all parties. It is the poverty of a closed economy, not free trade, that threatens ecological degradation around the globe.

Moreover, free market environmentalism provides a means for advancing both economic and ecological ends. It uses rather than suppresses the powerful incentives embodied in property rights and voluntary trade to better protect environmental and natural resources. As environmental concerns grow in importance in the global economy, so too will debate over this alternative vision. □

1. Larry Williams, "Mexican Trade Deal: Fallout or Fantasy?" *The Washington Times*, December 22, 1991.
2. *Journal of Commerce*, October 28, 1991, p. 5a; November 5, 1991, p. 8A.
3. Warren Brookes, "An Economic Silent Spring," *The Detroit News*, March 11, 1990.
4. David Morris, "The materials we need to create a sustainable society lie close to home," *The Utne Reader*, November/December 1989, p. 84.
5. Mikhail S. Bernstam, "The Wealth of Nations and the Environment," Institute of Economic Affairs, London, 1991.
6. Quoted in Fred Smith, "Environmental Quality, Economic Growth, and Trade," paper presented at the Cato Conference "Liberty in the Americas, Free Trade and Beyond," Mexico City, May 19–22, 1992.

Natural Controls

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Since natural laws govern the forces of life that created this universe in which we live, all of those laws are in harmony with each other. If man can learn more about them, and use them in his human and economic relations, he will learn to live in peace with his fellow men, and in harmony with his environment. . . .

As defined by one economist, economics is the science of making scarce materials go around. If we let it work, the natural system of economic law will provide that the scarce resources of earth continue to meet human needs.

It is when man intervenes to upset the workings of economic nature that he begins to have troubles. It is when he tries (always without success) to repeal natural laws—by artificial trade barriers, price controls, production quotas, inflationary policies, and other means—that we find ourselves destroying our natural resources and our environment.

—C. R. BATTEN

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DAVIS-BACON: JIM CROW'S LAST STAND

by John Frantz

The ugliest and most disturbing events in American history have usually been linked with state-sponsored or sanctioned racism: Incidents of police brutality, symbolized by the Rodney King trials. Slavery. The *Dred Scott* decision. The post-Civil War Jim Crow laws. School segregation.

Today, however, most people like to believe that their government fairly represents the interests of everyone, regardless of race. Unfortunately, the states and the federal government still discriminate against blacks, but this state-sponsored racism has taken on more subtle forms. Thus while great strides have been made since the Jim Crow era, some relics remain. One of them is the Davis-Bacon Act.

Davis-Bacon, passed in 1931, requires private contractors to pay "prevailing wages" to employees on all construction projects receiving more than $2,000 in federal funding. The Secretary of Labor is charged with conducting surveys of a region's wages and setting rates for up to 100 various classifications of workers. Most often, the "prevailing wage" corresponds to the union wage, especially in urban areas, where union membership tends to be higher. The Davis-Bacon Act covers approximately 20 percent of all construction projects in the United States and affects more than 25 percent of all construction workers in the nation at any given time.

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The Act was passed in order to prevent non-unionized black and immigrant laborers from competing with unionized white workers. The discriminatory effects continue, as even today minorities tend to be vastly under-represented in highly unionized skilled trades, and over-represented in the pool of unskilled workers.

Davis-Bacon restricts the economic opportunities of low-income individuals in a number of ways. Minority contracting firms are often small and non-unionized, and cannot afford to pay the "prevailing wage." The Act also requires contractors to pay unskilled laborers the prevailing wage for any job they perform, essentially forcing contractors to hire skilled tradesmen, selecting workers from a pool dominated by whites.

Thus, the Davis-Bacon Act constitutes a formidable barrier to entry into the construction industry for unskilled or low-skilled workers. This is especially harmful to minorities because work in the construction industry pays extraordinarily well compared to that for other entry-level positions, and could otherwise provide plentiful opportunities for low-income individuals to enter the economic mainstream.

In November 1993, the Institute for Justice, a Washington, D.C., based public-interest law firm, filed suit challenging Davis-Bacon constitutionality, as part of the Institute's litigation program to help restore judicial protection of "economic liberty"—the basic right to pursue a business or profession free from arbitrary government regulation.

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The History of the Davis-Bacon Act

Prior to the enactment of the Davis-Bacon Act, the construction industry afforded tremendous opportunities to blacks, especially in the South. In at least six southern cities, more than 80 percent of unskilled construction workers were black. Blacks also represented a disproportionate number of unskilled construction workers in the North, and constituted a sizable portion of the skilled labor force in both parts of the country.

This was so despite the fact that most of the major construction unions excluded blacks, and that blacks faced widespread discrimination in occupational licensing and vocational training. These unions felt seriously threatened by competition from blacks, and favored any attempt to restrict it.[1]

The co-author of the Act, Representative Robert Bacon, represented Long Island. Bacon was a racist who was concerned lest immigration upset the nation's "racial status quo." In 1927, he introduced H.R. 17069, "A Bill to Require Contractors and Subcontractors Engaged on Public Works of the United States to Comply With State Laws Relating to Hours of Labor and Wages of Employees on State Public Works." This action was a response to the building of a Veterans' Bureau Hospital in Bacon's district by an Alabama contractor which employed only black laborers.

Representative William Upshaw, understanding the racial implications of Bacon's proposal, stated: "You will not think that a southern man is more than human if he smiles over the fact of your reaction to that real problem you are confronted with in any community with a superabundance or large aggregation of negro labor."[2] Over the next four years, Bacon submitted 13 more bills to regulate labor on federal public works contracts. Finally, the bill submitted by Bacon and Senator James Davis was passed in 1931, at the height of the depression, with the support of the American Federation of Labor. The Act required that contractors working on federally funded projects over $5,000 pay their employees the "prevailing wage." The law was amended in 1935, reducing the minimum to $2,000 and delegating the power of determining the "prevailing wage" to the Department of Labor. The Department's regulations governing the determination of wages, remained basically unchanged for five decades and equated the prevailing wage with the union wage in any area that was at least 30 percent unionized. In practice, the "prevailing wage" was almost universally determined to be the same as the union wage.

The debate over Bacon's bills betrayed the racial animus that motivated passage of the law. Representative John Cochran stated, "I have received numerous complaints in recent months about southern contractors employing low-paid colored mechanics getting work and bringing the employees from the South."[3] Representative Clayton Algood similarly complained, "That contractor has cheap colored labor that he transports, and he puts them in cabins, and it is labor of that sort that is in competition with white labor throughout the country."[4] Other derogatory comments were made about the use of "cheap labor," "cheap, imported labor," "transient labor," and "unattached migratory workmen."[5] While supporters of the Act intended to disadvantage immigrant workers of all races, they were particularly concerned with inhibiting black employment.

Supporters of Davis-Bacon were also full of anti-capitalist rhetoric. Representative McCormack said of Davis-Bacon, "It will force the contractor who heretofore has used cheap, imported labor to submit bids based upon the 'prevailing wage scale' to those employed. It compels the unfair competitor to enter into the field of fair competition."[6] This rhetoric of "fairness" dominates much of the contemporary debate over Davis-Bacon, as well.

Two important modifications have recently been made in the way that the Davis-Bacon Act is enforced. In 1982, the Department of Labor altered the basis for determining the prevailing wage, deciding to equate the union wage with the "prevailing

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wage" only in places where the construction industry was 50 percent unionized. This change has had little effect on minority-owned firms' ability to secure contracts because union membership tends to be much higher in urban areas, where large minority populations reside.

The Department of Labor has also attempted to alter its regulations to allow contractors to hire a limited number of unskilled "helpers" to work on Davis-Bacon projects for less than the prevailing wage. This change, which was to go into effect on February 4, 1991, would help to diminish some of the discriminatory effects of the Act, but Congress has so far prevented the Department from enforcing it. Moreover, labor unions are now pressuring Congress and the Clinton Administration to repeal the changes. Similarly, while President Bush suspended the Act in South Florida, coastal Louisiana, and Hawaii in October of 1992 following Hurricanes Andrew and Iniki, President Clinton reversed course upon entering office.

Last year Senator Hank Brown (R-Col.) sponsored legislation to repeal the Davis-Bacon Act. A similar bill was introduced in the House by Representative Tom DeLay (R-Tex.). Both proposals have attracted congressional co-sponsors, but, not surprisingly, have failed to attain majority support.

Effects of the Davis-Bacon Act

The Davis-Bacon Act imposes tremendous economic and social costs—at least $1 billion in extra federal construction costs and $100 million in administrative expenses each year. Industry compliance costs total nearly $190 million per year. Repeal of the Act would also create an estimated 31,000 new construction jobs, most of which would go to members of minority groups.

Davis-Bacon's impact on the ability of minorities to find work in the construction industry has been particularly devastating. The Department of Labor's initial set of regulations did not recognize categories of unskilled workers except for union apprentices. As a result, contractors had to pay an unskilled worker who was not part of a union apprenticeship program as much as a skilled laborer, which almost completely excluded blacks from working on Davis-Bacon projects.[7] This effectively foreclosed the only means by which unskilled blacks could learn the necessary skills to become skilled workers.

As a result, while black and white unemployment rates were similar prior to passage of the Davis-Bacon Act, they began to diverge afterwards. This problem persists today. In the first quarter of 1992, the black unemployment rate was 14.2 percent, even though the overall national rate was only 7.9 percent.

The racial difference in unemployment rates is especially pronounced in the construction industry. According to a recent study by the National Urban League, in the fourth quarter of 1992, 26.8 percent of all blacks involved in the construction industry were jobless compared to only 12.6 percent of white construction workers.[8]

Despite recent racial progress, Davis-Bacon continues to inhibit minority economic progress in several ways. For instance, union apprenticeship programs, even if they no longer discriminate, still strictly limit the number of enrollees and impose arbitrary educational requirements on potential applicants, thereby excluding the most disadvantaged workers.[9]

Moreover, unskilled workers must be paid the same wage as a skilled worker, forcing the contractor to pay laborers considerably more than the market value of their work. For example, in Philadelphia, electricians working on projects covered by the Davis-Bacon Act must be paid $37.97 per hour in wages and fringe benefits. The average wage of electricians working for private contractors on non-Davis-Bacon projects is $15.76 per hour, with some laborers working for as little as $10.50 per hour.

Thus, even minority, open-shop contractors have no incentive to hire unskilled workers. Ralph C. Thomas, former executive director of the National Association of Minority Contractors, stated that a minority contractor who acquires a Davis-Bacon contract has "no choice but to hire skilled trades-

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men, the majority of which are of the majority." As a result, Thomas said, "Davis-Bacon closes the door in such activity in an industry most capable of employing the largest numbers of minorities."[10]

The paperwork a contractor must fill out pursuant to Davis-Bacon contracts also discriminates against small, minority-owned firms. Many do not have personnel with the necessary expertise to complete the myriad forms and reports required.

As a result of all these factors, the Davis-Bacon Act prevents rural and inner-city laborers and contractors from working on projects in their own communities. Ironically this is one problem Davis-Bacon was intended to prevent. Bacon said during debate over the Act, "Members of Congress have been flooded with protests from all over the country that certain Federal contractors on current jobs are bringing into local communities outside labor," and "that the government is in league with contract practices that make it possible to further demoralize local labor conditions."[11]

Such a claim could easily be made today by inner-city and rural contractors. Yale Brozen, an economist at the University of Chicago, found that the "prevailing wage" for the Appalachian region of western Pennsylvania is set at the same level as that of Pittsburgh, despite the fact that the wages normally paid by the rural contractors are only half the levels of union contractors in Pittsburgh. The same is true of inner cities, where small, minority-owned, open-shop firms are forced to pay union wages when working on Davis-Bacon projects, because of the high concentration of unionized workers in other parts of the city.

As a result, rural and inner-city contractors are deterred from seeking Davis-Bacon contracts because they cannot afford to pay the higher wages to their employees and larger and more highly unionized firms are encouraged to seek out such contracts. The result makes it clear that the government is in fact "in league with contract practices" that "demoralize local labor conditions," only now at the expense of minorities rather than whites.

The results of this practice were clearly demonstrated in Los Angeles. In the parts of the city where the riots occurred, the rate of unemployment for black workers is 27.6 percent. Despite an ample supply of local labor to help rebuild the city, Davis-Bacon has and continues to freeze out local unskilled minority workers from those available jobs. In contrast is the situation in South Florida and coastal Louisiana, where the suspension of Davis-Bacon created 5,000 to 11,000 jobs.

In addition to this statistical evidence, individuals involved in the construction and renovation of low-cost public housing have testified as to the disastrous effects of the Act. When Ralph L. Jones, president of a company that manages housing projects for the Department of Housing and Urban Development, gained control of a pair of dilapidated 200-unit buildings in Tulsa, Oklahoma, he intended to hire many of the building's unemployed residents to help restore the property. But the Davis-Bacon Act required him to pay everyone working on the project union wages, forcing him to hire only skilled laborers, very few of whom were minorities.

Mary Nelson, director of Bethel New Life, Inc., a social service organization located in Chicago, has found that Davis-Bacon adds up to 25 percent to her total costs and frequently prevents her from hiring unskilled, low-income workers to work on projects renovating the public housing that they themselves live in. Elzie Higginbottom, builder of low-income housing in Chicago's South Side, has had similar problems. Davis-Bacon requires him to pay carpenters (defined by the Act as someone who hammers in a nail) $23 per hour. As a result, he complained, "I've got to start out a guy at $16 per hour to find out if he knows how to dig a hole. I can't do that."[12]

Conclusion

The constitutional challenge to Davis-Bacon is a cornerstone of the Institute for Justice's program to restore economic liberty as a fundamental civil right. The Insti-

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tute is challenging Davis-Bacon on the grounds that it is racially discriminatory, since it was passed to discriminate against blacks and immigrants, and as a result, violates the equal protection guarantee of the Fifth Amendment. The courts need only look to the legislative and administrative history of the law to determine that racial discrimination was among its purposes. The courts could also void the Davis-Bacon Act for impinging on the right of individuals to pursue employment opportunities, thereby violating the Fifth Amendment's due process clause. The Institute for Justice has brought together a unique coalition of plaintiffs to challenge the law. Complainants range from individual minority contractors, who have either lost opportunities to successfully acquire government contracts or who have gone out of business altogether because of the application of Davis-Bacon, to resident-management corporations who because of the law have been unsuccessful in their attempts to involve public-housing residents in rebuilding programs at their own developments.

Borne of racial animus, the Davis-Bacon Act has undermined the efforts of economic outsiders to find employment in the construction industry for more than six decades. Given the influence of organized labor over Congress and the extent to which the Clinton administration's support of NAFTA alienated this key constituency, it is highly unlikely that either branch will risk further undermining union support by pursuing reform or repeal of the Davis-Bacon Act. Thus, the only avenue that remains open is the judiciary. The courts should bury this relic of the Jim Crow era. □

1. Johnson, "Negro Workers and the Unions," *The Survey*, April 15, 1928.
2. *Ibid.*, p. 3.
3. *Employment of Labor on Federal Construction Work*, Hearings on H.R. 7995 and H.R. 9232 Before the House Committee on Labor, 71st Congress, 2nd Session, March 6, 1930, p. 26–27.
4. *Rates of Wages for Laborers and Mechanics on Public Buildings of the United States*, *74 Congressional Record* 6504, 6513, (1931).
5. *Ibid.*, pp. 6515-6520.
6. *Employment of Labor on Federal Construction Work*, p. 6516.
7. *Ibid.*, p. 4.
8. National Urban League, *Quarterly Economic Report on the African American Worker*, Fourth Quarter, 1992, Table 7 (presently unpublished).
9. John Gould and George Billingmayer, *The Economics of the Davis-Bacon Act*, (Washington, D.C.: American Enterprise Institute, 1980), p. 62.
10. Testimony by National Association of Minority Contractors before House Subcommittee on Labor Standards of the Committee on Education and Labor, Sept. 30, 1986, p. 3.
11. *Employment of Labor on Federal Construction Work*, p. 6511.
12. Patrick Barry, "Congress's Deconstruction Theory," *The Washington Monthly*, January, 1990, p. 11.

IDEAS ON LIBERTY

Why Does Davis-Bacon Persist?

The harmful effects of the Davis-Bacon Act do not seem to impair its popularity. They are interpreted away and placed on the doorsteps of capitalism. The American public does not suspect the Davis-Bacon Act, the Norris-LaGuardia Act, or the Smoot-Hawley Tariff Act of having played an ominous role in the Great Depression. It lays the blame instead on mysterious failings of the private-property order and the profit motive. It does not suspect labor legislation of causing unemployment, especially among minorities. Instead, the public is persuaded that white middle-class racism, especially among employers, is responsible for the unemployment plight.

To raise the income of labor by legislative fiat or union coercion is the very essence of interventionism. In the eyes of the American public, to raise wages is virtue, to take from employers is morality. In the world of reality, however, inexorable economic principles contradict such notions and point up the inevitable consequences of policies based on these notions. In economic life, principle must prevail in the end.

—Hans F. Sennholz

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THE FREEMAN
IDEAS ON LIBERTY

FEDERAL TRANSIT SUBSIDIES: HOW GOVERNMENT INVESTMENT HARMS THE U.S. ECONOMY

by John Semmens

It has been asserted by some that part of what is needed to revitalize the U.S. economy is more government investment. There is, of course, a superficial plausibility to this assertion. Every dollar the government spends becomes somebody's income. The people working on government-funded projects do have jobs. The purchases government makes result in revenues for some businesses. All of this is formalized in the Gross National Product (GNP) wherein every monetary transaction that takes place is tallied as one measure of the economy's health.

If we are to make an intelligent assessment of the potential impact of a prospective increase in government investment, though, we will need to do more than rely upon the superficial plausibilities. After all, throwing money out of the windows of the U.S. Mint would also provide a superficially plausible stimulation of the U.S. economy. People would catch the windblown currency and spend it on something. This spending would become someone else's income. It would support jobs. It would even show up in GNP statistics. However, few, save Keynesian diehards, would tout currency tossing as a legitimate government investment program.

A traditional first step in analyzing any investment is to examine the historical performance record. Since one of the most frequently mentioned public sector investments is increased public transit subsidies, perhaps it would be worth our while to investigate the historical performance of federal aid for transit. While there is no guarantee that future performance would duplicate past performance, many professional investors regard historical informa-

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Table 1
Impacts on the U.S. Economy of Alternative Investments
($ in Billions)

	Public Transit	Corporate Tax Cut	Capital Gains Tax Cut	IRA: Treasury Bills	IRA: S&P 500 Stocks
Amount Invested	$61.5	$61.5	$61.5	$61.5	$61.5
Current Value	$10	$100	$160	$130	$250
Impact on GNP	$40	$400	$650	$500	$1000
# Jobs	800,000	8 mil.	13 mil.	10 mil.	20 mil.
Federal Taxes	$8	$75	$120	$100	$190

Sources: *Economic Report of the President* (January 1993)
Statistical Abstract of the U.S. (1992)
Transit Fact Book (American Public Transit Association)

tion as indicative of what to expect in the future.

The proponents of government investment in public transit are hardly modest in the claims they make for the economic benefits to be gained from such investments. For its part, the American Public Transit Association (APTA) boasts that every dollar spent on public transit generates three to five dollars of additional economic activity. In 1984, the APTA issued a report entitled *National Impacts of Transit Capital and Operating Expenditures on Business Revenues*. This report asserted that every dollar spent on rail transit produced $3.15 in added business revenue. For every dollar spent on bus transit, the APTA report estimated that an additional $3.50 in business revenue was generated.

In 1991, another APTA report—*Transportation Spending and Economic Growth: The Effects of Transit and Highway Expenditures*—claimed even more robust returns from transit outlays. In this case, for every dollar spent on transit an estimated $5.20 in additional economic activity was alleged to result.

These impacts of three and five to one certainly sound impressive. It is easy to see how some people could become enthusiastic about this seeming fount of prosperity. However, it is important to remember that all expenditures of money generate similar ripple effects through the economy. Whether putting our money into public transit is a good or a bad investment depends upon the return we get on the investment. Before we rush to plow more billions into transit it might be wise to compare this particular investment to alternative ways the same money could have been invested.

Looking at Investment Alternatives

The figures shown in Table 1 indicate the potential returns the U.S. economy might have experienced if the tax dollars that went into public transit had been invested differently. For this analysis, I have assumed that the $61.5 billion that the federal government has invested in public transit between 1965 and 1992 would have been put into any of several obvious alternatives. The annual federal cash flow into transit over this time period is assumed to have been directed instead into each of the four alternatives portrayed in the table.

The "amount invested" is the same $61.5 billion for each alternative. The "current value" is the estimated current value of the assets for each investment alternative as of the end of 1992. The "impact on GNP" is the estimated 1992 amount of economic activity that has been (or would have been) added to GNP by each investment alternative. The "# jobs" is the estimated number of employment opportunities that could be supported by the economic activity generated by each investment alternative in 1992.

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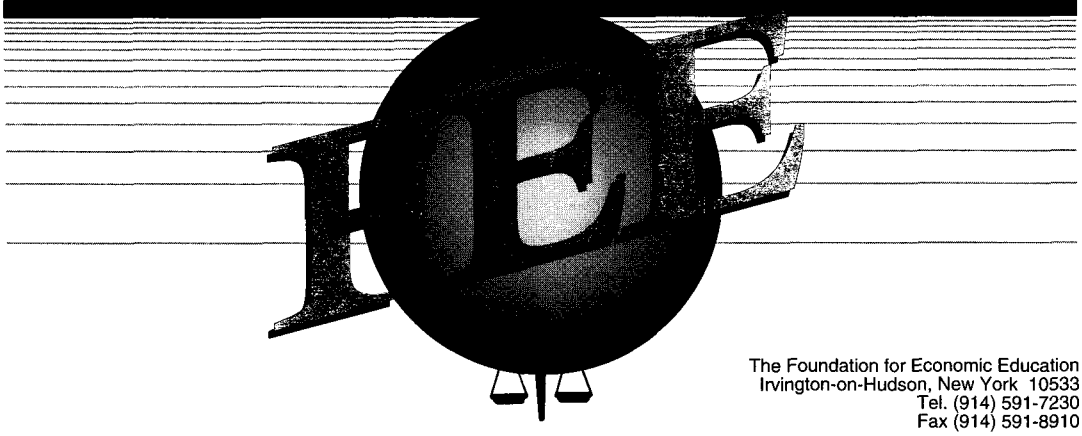

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February 1994

Freedom Has Many Enemies

Most people long for freedom — social, economic, political, mental, and spiritual. It strengthens their energy, invigorates their intellect, sustains their virtue, and permits them to pursue their own good, in their own way. Yet, no matter how salutary freedom may be, it has many enemies. There is evil in the human heart which tempts man to take advantage of the weakness of others and deprives them of their freedom. Many men love power which is the root of much oppression.

Power tends to intoxicate the best heart; it dazzles the mind, and steals the freedom from the many to the few. Power pollutes whatever it touches. Few legislators, regulators, and public officials who wield much power over their fellow men can resist the temptations of power pollution. In the words of Edmund Burke, the eminent British political writer and statesman, "The greater the power the more dangerous the abuse."

In an economic command system, whether it be socialistic or fascistic, much economic power rests in the hands of an economic czar. It is unlikely that he and his entourage will ever champion the cause of individual freedom; it is probable, instead, that they will progress to the extremes of tyranny. The lust of power is innate in government officials; it is the strongest of all the passions.

Human nature is the same in all locations and situations. Democratic governments may commit as many flagrant acts of tyranny as despotic governments, especially if they engage in policies of massive economic transfer and welfare. They do not enlist the friends of freedom. The agencies and bureaus, authorities and commissions are staffed with detractors, antagonists, and enemies of freedom. They are led by many legislators, regulators and tax collectors who are deaf to the meaning of freedom.

The legions of bureaucrats who control and regulate our economic lives do not favor decontrol and deregulation. They do not advocate reductions in taxation which is the very source of their livelihood. There are few, if any, bureaucrats who plead for tax reductions and cuts in their incomes.

There are public school teachers and many other tax consumers who do not wield much power. But their income and livelihood depend on the power to tax the public. Thousands of professors and administrators at state colleges and universities thrive on revenue forcibly extracted from taxpayers. Surely, it must be difficult for them to hold forth on the evils of government coercion while enjoying government largesse. To justify their pickings, they are likely to defend the system. But if taxation for the purpose of education is consistent with the principles of freedom, is it not equally consistent for purposes of transportation, information, entertainment, healthcare, retirement, and a hundred other pursuits? There are few public educators who would not answer this question

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in the affirmative. They are preparing their charges for a comprehensive command system commonly called socialism.

In 1992, for the first time in U.S. history, the number of government employees who lived on tax revenues exceeded the number of workers in manufacturing industries. If both groups should consistently vote their income interests, the outcome would be clear: ever higher taxation and lower margins of freedom.

The army of federal, state, and local personnel receives much reenforcement from an even larger army of transfer beneficiaries. The federal government conducts major transfer policies benefiting many millions of recipients who cannot be expected to cast their votes against the transfer system. The two main categories of transfer are "means-tested programs" and "social insurance". The former provide benefits or services to people whose income has fallen below certain levels. The latter compensates people for income loss due to retirement, disability, and unemployment, and provides health insurance for the elderly.

Means-tested federal expenditures presently exceed $6,000 per person, rising at a rapid rate especially through Medicaid spending. The Federal Aid to Families with Dependent Children program (AFDC) assists more than twelve million people. The Supplemental-Security Income (SSI) program provides benefits to more than five million recipients, and the earned income tax credit program helps more than thirty-three million people. Means-tested noncash transfer programs include Medicaid, which benefits some twenty-six million people, the food stamp program, which subsidizes some twenty-two million people, the Head Start program for half a million 3- and 4-year olds, and the Pell Grant Student program, which assists nearly four million students.

Social Security, which covers more than 90 percent of all adult Americans, provides monthly payments to more than forty-two million people of whom some twenty-six million are retired workers receiving average monthly benefits of some $1,100. Nearly four million individuals draw benefits from the Federal Employee Retirement System and more than four million from state and local retirement systems. And, under the Medicare program, more than twenty-five million elderly and disabled beneficiaries presently enjoy an average of $4,000 of medical benefits individually, or some $100 billion collectively.

It is difficult to imagine how individual freedom can survive the onslaught of these recalcitrant forces. Yet the cause of freedom is not hopeless because the armies of bureaucrats and beneficiaries rarely form a united front. They bicker and wrangle among each other, take sides, and occasionally may even choose freedom. The public school teacher may opt for private medical care and the Medicare doctor for private education. The retired bureaucrat may oppose Pell grants to students and the students retirement benefits for bureaucrats. The Medicaid patient may object to Medicare benefits for millionaires, and the millionaires to Medicaid benefits for illegal aliens. Indeed, the Social Security recipient may sincerely espouse the cause of freedom except in matters of Social Security. And the state college professor may wax eloquent about the virtues of freedom except in matters of college education.

Consistent champions of freedom are extremely rare. The only thing in which men are consistent is inconsistency. They hold fast to their principles on one issue and cling to another on different issues. Yet, the spark of freedom is in every human heart. It may break into flames despite all the temptations and entitlements that seek to extinguish it.

Hans F. Sennholz

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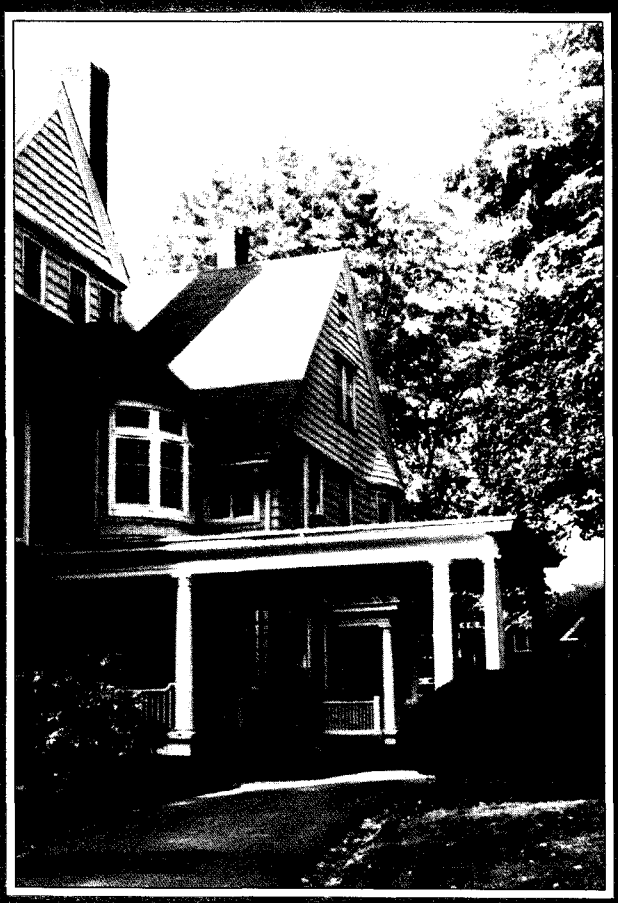

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Edmund Opitz, an ordained Congregational minister, founder of The Remnant (a fellowship of conservative and libertarian ministers) and The Nockian Society, is an associate editor of *The Freeman.* He served as a member of the senior staff of FEE from 1955 until his retirement in 1992. *Religion: Foundation of the Free Society* is vintage Opitz, graced with his elegant style, subtle wit, and gentle erudition.

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The "federal taxes" are the estimated additional tax revenues accruing to the federal government during 1992 as a result of the economic activity generated by each investment alternative.

The "public transit" investment option is, of course, the actual government investment made during this time period. The "corporate tax cut" investment option assumes that the amount spent on transit would have been "spent" on corporate tax relief (for example: an investment tax credit or a cut in corporate income taxes) and that this money would have been invested in business assets earning average rates of return. The "capital gains tax cut" investment option assumes that the amounts spent on transit subsidies would have been "spent" on reducing the capital gains tax and that this money would have been invested in the stocks comprising the Standard & Poor's 500 stock index. Dividends were not assumed to be reinvested. The "IRA: treasury bills" investment option assumes that the amount spent on transit would have been "spent" by allowing tax-free investing by individuals and that these individuals selected a very conservative investment strategy of buying three-month treasury bills. The "IRA: S&P 500 stocks" investment option assumes the same tax-free investing by individuals, but that they buy stocks. In this case, dividends are assumed to be reinvested.

The comparison of these investment alternatives is quite startling. The contributions to the U.S. economy made by public transit are pathetically meager compared to any of the alternatives. Even the least favorable private sector investment alternative could have had an incremental impact on the U.S. economy ten times the size of that the actual public transit investment has had. If any of these alternative paths had been chosen, GNP would have been larger, more people would have jobs, and the federal deficit would have been lower.

Recent statistics indicate that there are about 9 million persons classified as unemployed. The implication of our analysis of hypothetical investment alternatives is that unemployment problems would have been greatly reduced had the government made different investment decisions. The more lucrative returns of the alternative investments would have created more job opportunities. More people would have been attracted into the workforce. Wages would likely have risen. The additional capital that would have been available would likely have improved labor productivity. So, even if it does seem improbable that the economy could sustain an additional 20 million jobs, as the "IRA: S&P 500 stocks" option implies, it is obvious that the employment environment would be far more favorable than it now is.

The projection of a lower federal deficit is predicated on the assumption that all other expenditures remain the same. This probably tends to understate the favorable impact that a different investment decision would have had. Surely, the more robust employment environment that could have existed would be expected to reduce government outlays for unemployment compensation and welfare. Likewise, the higher tax revenues that the government would have received would also have reduced borrowing costs. These factors could have lowered the deficit even more than the additional tax revenues projected in Table 1 would imply.

Profits Instead of Deficits

The reason why each of the prospective investment alternatives would have produced much better results for the U.S. economy than the transit investment that was made is that each alternative would have earned a profit. Public transit does not earn a profit. As a whole, it cannot even cover its operating costs from passenger revenues. A glance at a graph of the aggregate public transit operating results from 1965 to 1992 (see Figure 1) shows a trend of deepening annual deficits. The losses suffered by public transit mean that the value of the outputs of the investment are worth less than the cost of the inputs. What this means is that the money invested in public transit is *consumed*. The investment cannot sustain

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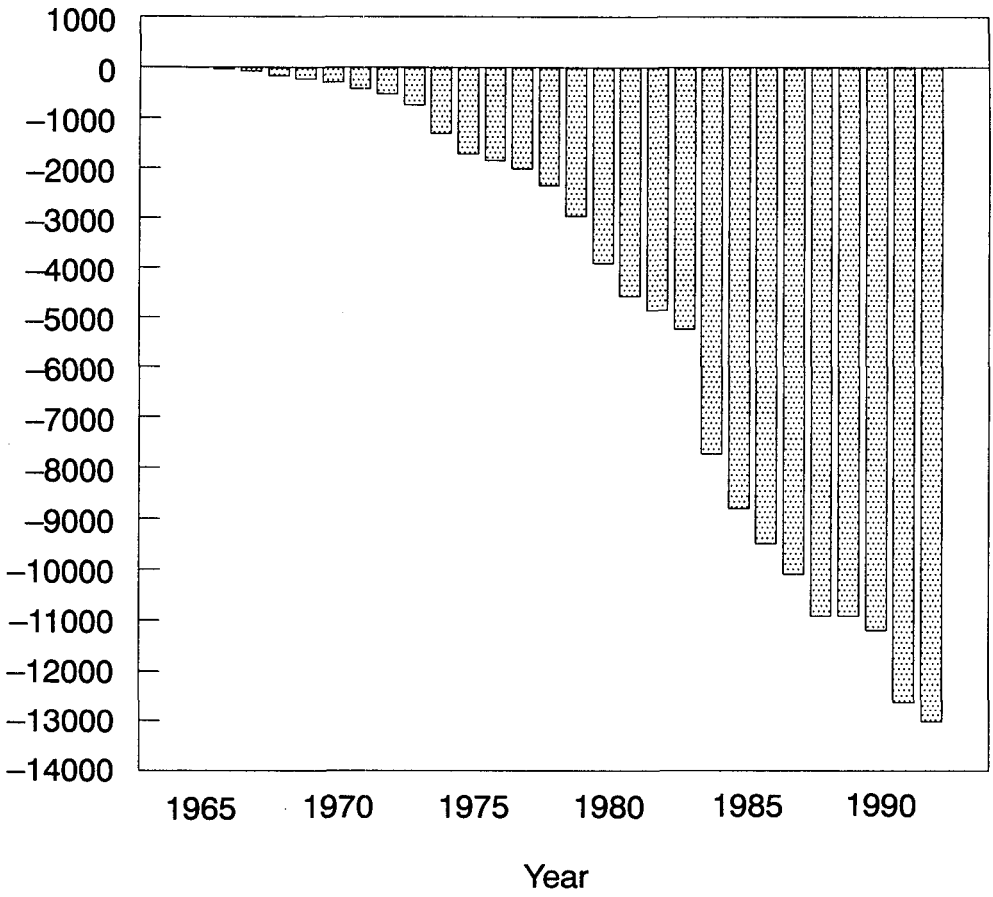
FIGURE 1
ANNUAL PUBLIC TRANSIT DEFICITS
(IN MILLIONS OF DOLLARS)



Source: Transit Fact Book (American Public Transit Association)

itself independent of continual infusions of new capital.

The superior performance of the alternatives comes from the compounding of profits made on the capital invested. These profits mean that the value of the outputs of the investment exceed the cost of the inputs. Consequently, the money invested grows with each increment of profit. The process of making a profit on an investment enables one to end up with more wealth than he had when he started. Greater wealth, of course, would make the U.S. economy stronger and better able to meet the material needs of more people.

The last gasp of a defense on behalf of money-losing government investments like public transit is that a needed service is provided. Unfortunately, the fact that public transit is subsidized makes it impossible to determine the need for the service. The fact that we do not ask the consumers of public transit to pay what it costs to provide the service denies us any objective measure of need. It is probable that a substantial portion of the so-called need for transit would dissipate if taxpayers were not paying over 60 percent of the cost of every transit ride.

While the need for money-losing transit has been undemonstrated and exaggerated, the need for the products and services that

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would have been provided by the forgone alternatives is easily overlooked. The fact that consumers of unsubsidized products and services produced by the private sector do pay the full costs is proof that a need has been fulfilled. The voluntary payment by willing consumers is an objective measure of need. So, not only has the federal government's 27-year investment in public transit lost money, it has also prevented trillions of dollars worth of needs from being fulfilled.

The federal government's investment in public transit currently amounts to around $3 billion per year. This is a relatively small amount of spending. But as we have seen, the cumulative economic cost of annually pouring a small amount of money into profitless transit operations in the past has had a huge opportunity cost for the U.S. economy. To place the total negative impact of excessive government spending in perspective, consider that the Grace Commission estimated that there was $140 billion per year in unnecessary federal spending. As this process of waste continues year after year the compound effect on the U.S. economy has to be devastating.

The inability of the federal government to contain its appetite for bad investments has been a disaster of major proportions. The competitiveness of U.S. businesses, the standard of living of the population, even the health, safety, and welfare of the American people have been enormously harmed by the inferior investment choices policymakers have made over the last generation.

When we see what could have been and compare it to what is, we are observing a government performance worthy of shame, not repetition. Unless we want to repeat and intensify this shame, it is clear that more government investment is exactly what we don't need. □

PRIVATE HIGHWAYS IN AMERICA, 1792-1916

by Daniel B. Klein

Fifteen years ago only technology aficionados and laissez-faire idealists entertained the notion of private highways. Today, however, public officials and entrepreneurs are struggling to make the notion a reality. Four private highway projects are underway in California and many other states are following suit.

The notion of private highways, which would seem fantastic to our parents, was commonplace to our great-great-grandparents. Initiated in the 1790s in the growing Republic, these roads stimulated commerce, settlement, and population. During the nineteenth century more than 2,000 private companies financed, built, and operated toll roads. States turned to private initiative for much the same reason they are doing so today: fiscal constraints and insufficient administrative manpower. Knowledge of our toll-road heritage may

Dr. Klein is an assistant professor of economics at the University of California, Irvine.

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Table 1
Turnpike Incorporation, 1792-1845

State	1792–1800	1801–10	1811–20	1821–30	1831–40	1841–45	Total
New Hampshire	4	45	5	1	4	0	59
Vermont	9	19	15	7	4	3	57
Massachusetts	9	80	8	16	1	1	115
Rhode Island	3	13	8	13	3	1	41
Connecticut	23	37	16	24	13	0	113
New York	13	126	133	75	83	27	457
Pennsylvania	5	39	101	59	101	37	342
New Jersey	0	22	22	3	3	0	50
Virginia	0	6	7	8	25	0	46
Maryland	3	9	33	12	14	7	78
Ohio	0	2	14	12	114	62	204
Total	69	398	362	230	365	138	1552

Source: Klein & Fielding, *Transportation Quarterly* (1992)

help encourage today's budding toll-road movement.

The Turnpike Heyday, 1800-1825

Once the state of Pennsylvania chartered a private company in 1792 to build a road connecting Philadelphia and Lancaster, rival states felt impelled to follow. Private initiative was the only effective means of providing new highways, because state and county finances were almost nonexistent and town resources were meager. Private control and user fees were bold steps, but once taken, states could only continue to move forward. In an age before the canal and railroad, legislators were willing to test community and political custom to get highways built.

The turnpikes were financed by private stock subscription and set up to pay dividends. Built with a surface of gravel and earth, turnpikes were usually 15 to 40 miles in length, and cost $2,000 per mile to build. They were massive undertakings and relied on widespread investment from the community. Stock purchased was more like a contribution to community improvement rather than a business investment. Some travelers objected to the idea of paying tolls, particularly to a corporate monopoly. Legislators, often suspicious of corporate motives, wrote extensive (and economically debilitating) restrictions into company charters, specifying conditions for construction, maintenance, and toll rates, and toll collection.

The progress of turnpike incorporation is shown in Table 1. Only Pennsylvania, Virginia, and Ohio subsidized their turnpike companies; New York chartered the most turnpikes. The opening decade of the nineteenth century saw the most charter activity, though roughly one-third of the companies chartered failed to construct a single mile of roadway.

The unprofitability of turnpikes soon became obvious. The vast majority of turnpikes paid only very small dividends or none at all. First, toll evasion was rampant, as people would circumvent tollgates—a practice known as "shunpiking." Second, many roads were built in advance of settlement and travel demand was low. Third, legal restrictions and regulations, limiting both toll rates and countermeasures to shunpiking, hamstrung the turnpikes' abilities to improve their financial situation.

But poor financial returns did not necessarily mean unfruitfulness. Even an unprofitable turnpike stimulated commerce, raised land values, and aided expansion. Therefore, community leaders resorted to a fascinating array of tactics to boost the turnpike cause despite the sad prospects for

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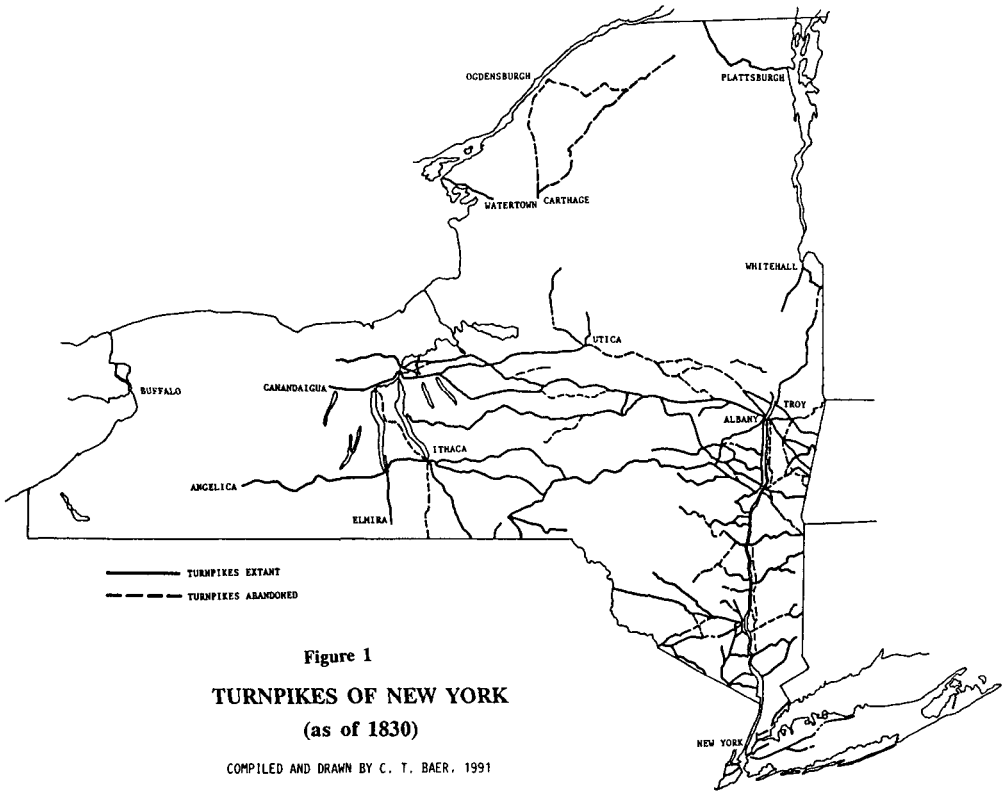

Figure 1

TURNPIKES OF NEW YORK

(as of 1830)

COMPILED AND DRAWN BY C. T. BAER, 1991

dividends. Supporters used newspaper appeals, town meetings, door-to-door solicitations, and correspondence to apply social pressure. In this way as in others, American communities relied on voluntarism, as so elegantly described by Alexis de Tocqueville, to meet local needs. The result in terms of turnpike construction in New York is shown in Figure 1.

Canals, Railroads, and Spur Turnpikes, 1826-1845

In the late 1820s canals began competing with many of the major turnpikes. Railroads joined in a bit later. Between 1825 and 1845 turnpike mileage dropped considerably. At the same time, however, the canals and railroads changed the patterns of trade and development, and stimulated new demands for shorter toll roads that would serve as feeders. Table 1 shows that turnpike activity by no means ceased with the advent of canals and rails.

Plank Road Fever, 1847-1853

High hopes for a new kind of short feeder road were placed in the idea of plank roads, organized like turnpikes but surfaced with wooden planks. Plank surfacing promised a smooth, inexpensive alternative to turnpikes, which sometimes resembled a river of mud. Plank road fever struck in the late 1840s and thousands of miles of plank roads were constructed.

Civil engineers and enthusiasts predicted that plank roads would last eight years before needing to be resurfaced. Beginning in 1847, rural Americans financed and constructed plank roads in massive numbers. Table 2 shows total incorporation for sev-

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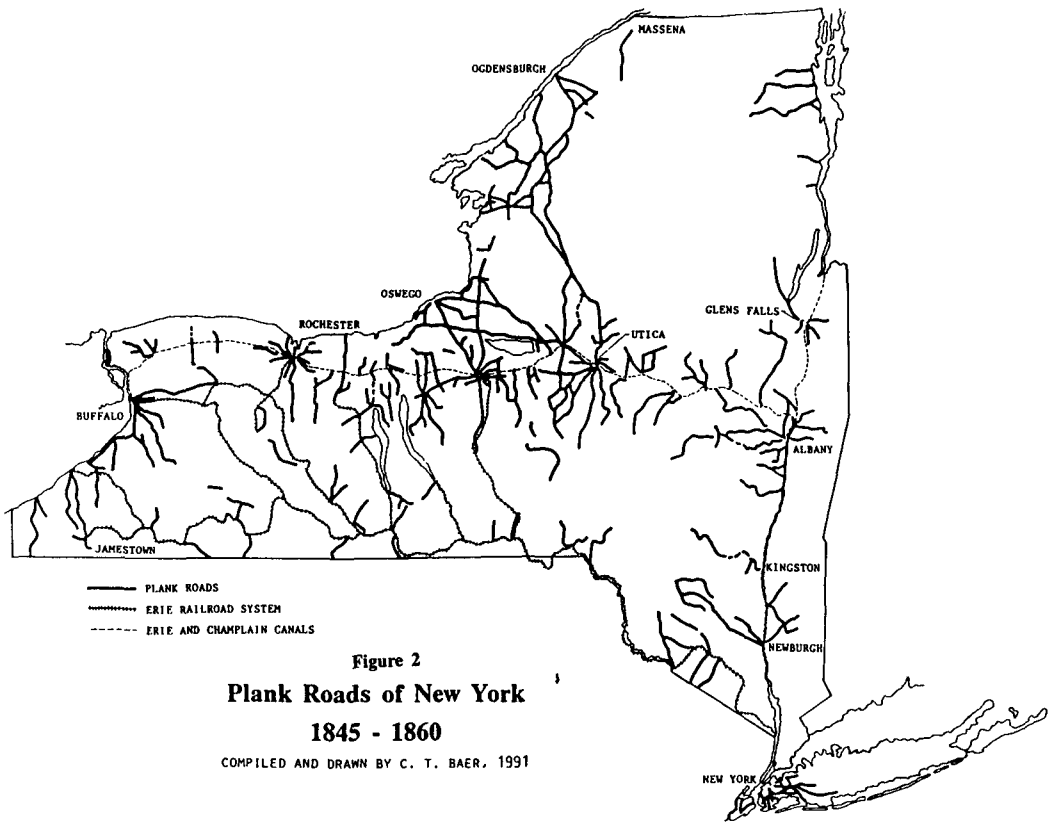

Figure 2
Plank Roads of New York
1845 - 1860
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eral states. Figure 2 shows the plank road system in New York.

But the planks wore out twice as fast as predicted—usually within four years. The movement ended as suddenly as it had begun. Most plank road companies folded, while others converted their operations to gravel turnpikes.

Toll Roads in the Far West, 1850-1890

The toll road idea endured to the end of the century. Discoveries of gold, silver, copper, and other minerals in California, Colorado, and Nevada sparked rushes of newcomers. Even before statehood for Colorado and Nevada entrepreneurs organized their own toll road enterprises to serve the mining communities, and some got rich in the process. Well over 360 toll roads were constructed in California, Colorado, and Nevada alone. This experience indicates that private initiative can provide infrastructure for economic development—so long as government respects people's liberty to do so.

The Good Roads Movement and the End of the Toll Road, 1890-1916

By the end of the nineteenth century, state and county governments had grown in capabilities and new agencies began setting goals for centralized highway management. Independent private toll roads were not thought appropriate in the era of progressive governance, and most of those remaining were bought out or shut down. Observed a county board in New York in 1906:

> The ownership and operation of this road by a private corporation is contrary to public sentiment in this county, and [the] cause of good roads, which has received

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Table 2
Plank Road Incorporation by State

State	No.	State	No.
New York	350	Georgia	16
Pennsylvania	315	Iowa	14
Ohio	205	Vermont	14
Wisconsin	130	Maryland	13
Michigan	122	Connecticut	7
Illinois	88	Massachusetts	1
North Carolina	54	Rhode Island	0
Missouri	49	Maine	0
New Jersey	25		

Notes: Ohio is through 1852; Pennsylvania, New Jersey, and Maryland are through 1857. Few plank roads were chartered after 1857.

Source: Majewski, Baer & Klein, *Journal of Economic History* (1993).

so much attention in this state in recent years, requires that this antiquated system should be abolished. . . . That public opinion throughout the state is strongly in favor of the abolition of toll roads is indicated by the fact that since the passage of the act of 1899, which permits counties to acquire these roads, the boards of supervisors of most of the counties where such roads have existed have availed themselves of its provisions and have practically abolished the toll road.

Conclusion

In 1991 Congress passed the Intermodal Surface Transportation Efficiency Act (ISTEA), which changed the 75-year policy against toll roads. It permits the use of federal funds on toll roads, including ones designed, constructed, and operated by private groups. It sheds the old requirement that states repay federal funds if the facility is transferred to private control. Although highway financing should be strictly private, ISTEA greatly improves the present system, which relies on unpriced highways built and operated by government. Under ISTEA, America might begin to rediscover the effectiveness of private management and the economic virtue of user charges. With new electronic technologies of toll collection, toll roads make more sense than ever.

As we enter the potentially new era of privately managed highways, the historical experience with toll roads offers some important lessons. First, private operation is more flexible, creative, and motivated to serve than government control. In the nineteenth century, private road companies consistently out-performed their public-sector alternatives. Second, private roads will not be constructed without the prospect of private gain. If governments over-regulate or renege on their promises, private road development will not occur. Finally, infrastructure is an economic good best left to private action.

Private roadways have always made philosophical sense. Now even many public officials understand that they make economic sense as well. □

If Men Were Free to Try

IDEAS ON LIBERTY

How could roads be built and operated privately? I do not know. This is a subject to which none of us directs his creative attention. We never do think creatively on any activity pre-empted by government. It is not until an activity has been freed from monopoly that creative thought comes into play. . . .

—JOHN C. SPARKS (1954)

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THE FREEMAN
IDEAS ON LIBERTY

HUMAN RIGHTS AROUND THE GLOBE

by Tibor R. Machan

It is interesting that so many people find the humanities, especially philosophy, irrelevant. People have always resisted philosophy. In our time it is often the so-called practical professionals who regard thinking about the great questions a waste of time and would rather handle problems piecemeal, on the spur of the moment, with no consideration of the big picture.

Yet no sooner does someone attempt to defeat philosophy than philosophy tends to win. Philosophy is, after all, trying to make sense of the world, of seeking, with spirit and determination, to attain wisdom, to live the examined life. And even those who set out to deny its value get trapped by philosophy—their denial is itself an attempt to reach wisdom, namely, that seeking wisdom isn't wise, so it's wiser to give it up!

This was evident at the June 1993 international human rights conference held in Vienna, Austria, where the assembled heads of governmental and non-governmental organizations debated human rights. One of the most troubling topics of the conference was what human rights are. When we speak of human rights, are these conditions that everyone everywhere ought to enjoy? Should these same basic conditions be protected by governments everywhere in the world? Or are human rights one thing for people in one part of the globe and another for those in another part?

Many leaders of Third World countries—where various types of dictatorships still flourish—argue, predictably, that human rights should not be understood the same way in Western democracies and their own societies. Why? Because their societies, they say, require greater regimentation, more state interference, and pervasive government planning in order to survive. This really means, of course, that because those in power in such societies have goals and purposes that require subjugating others, they don't believe that the concept of human rights—to liberty, autonomy, full political participation, civil rights, religious worship, freedom of the press—should apply.

There are, of course, cultural differences that should be honored. But they do not concern rights, which are basic principles of human community life. Cultural differences are valid only where they include peaceful practices, customs, mores, etiquette, styles, and tastes. Different cultures often exhibit certain prominent temperaments that prevail in a society. The Scandinavians are often more quiet and collected than Latins. The Finns are more melancholy than the French. Verbosity, reticence, even shyness can be matters of temperament, the kind of benign difference that is important for an individual's life. And there is much diversity in the arts of different cultures, based on

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different histories, climates, and other factors.

But human rights are based on universal human attributes. Indeed, universal human rights concern the basic freedoms that people ought to have protected so as to make peaceful choices for themselves in all walks of life. And it is only if such rights are given full protection that the valuable differences based on the highly diverse circumstances in people's lives can be fully exploited and realized. □

JURY NULLIFICATION: CORNERSTONE OF FREEDOM

by Roger Koopman

"The Jury has the right to judge both the law and the fact in controversy." That statement was penned not by some modern-day political theorist, but by John Jay, first Chief Justice of the United States Supreme Court. It did not reflect some quaint or offbeat ideology, but rather, the consensus of opinion at the founding of our nation. Our Founding Fathers understood that the constitutional republic they had crafted was a fragile thing. Without the proper safeguards, it could in time fall prey to tyranny masquerading as law. They recognized that one of the most essential of safeguards was the power vested in the common citizen through the jury box.

If our nation's founders were able to come back today and witness the instructions that judges lay upon the juries, they would react with horror at the emasculation of our once-proud jury system. Indeed, it bears little resemblance to the system they established, precisely because its most essential ingredient—the individual, independent juror—has largely disappeared. The juror is instructed to accept the letter of the law without question, and apply no moral judgment to his decisions. To the nation's founders, today's jury system would appear as nothing more than a ghost of its former self.

They would wonder how we managed to stray so far from the original pattern they instituted and why, as a result, America has chosen to place her freedoms in such obvious peril. Our forefathers, it seems, understood far better than we that for a nation to remain free, sovereign power must rest in the people themselves. They designed the jury system to act as a constant check on the excesses of government and the abuses of unjust law. Individual jurors acknowledged that they had not only the authority, but the moral responsibility to acquit just men who ran afoul of unjust law.

Throughout the history of our republic, there have been many instances of juries that stood firmly for justice in the face of illegitimate law. They commonly refused,

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for example, to enforce the British Navigation Acts against the colonists and later, the Fugitive Slave Act against the abolitionists. American history would have been written much differently if the juries of the past functioned like the juries of the present. Sadly, a modern-day jury would toss those abolitionists in jail, not because we now believe in slavery, but because juries today are consistently misinformed from the bench about their essential role in securing justice, and are thus rendered impotent in the defense of freedom. They are instructed to determine the facts, apply the law, and go home.

The "Fully Informed Jury"

It is ironic, then, that proposals to require juries to be informed of their vested powers are characterized as "radical." There is nothing radical about recognizing the wisdom of our Founding Fathers and reestablishing those sound principles of justice which we have allowed, through carelessness and neglect, to slip away. The so-called "fully informed jury" is at the bedrock of our republic.

It is important to recognize that this concept does not create any "new" powers, rights, or privileges. It merely asserts those jury powers and rights that have long existed. Simply stated, the proposal requires that juries once again be apprised of their inherent right to judge not only the facts of a case, but the law itself as it relates to that case.

As a practical matter, fully informed juries would result in little or no change in the great majority of all jury decisions. But in the few cases where juries asserted themselves and to some degree judged the law itself, they would help both secure justice and maintain a free society. Over time, if juries consistently "nullified" certain statutes by refusing to convict defendants, juries would be sending a powerful message to the legislative branch. The "sovereign" (the people) would have spoken, making an unjust law unenforceable and dramatically demonstrating that the law should be amended or repealed.

Jury nullification could also act some day as a vital defense against oppressive federal laws criminalizing behavior that is no crime. Consider if, for example, Congress voted to ban gun ownership. Ninety percent of those living in my home state of Montana would instantly become "law-breakers," yet none would be viewed by their neighbors as having committed any "crime." If Montana juries were informed of their true powers, it would be impossible to convict a Montanan who was simply exercising his Second Amendment rights. But this kind of check on abusive governmental power requires that juries be well informed.

Of course, juries could refuse (and occasionally have refused) to enforce just laws. But such cases are likely to be rare since most people agree on the government's basic duty to protect life, liberty, and property.

Once "informed juries" started cleansing the system of unpopular and repressive laws, two changes would begin to take place among the people themselves. First, people's respect for law itself (something that has declined in recent years, largely because of the mischief caused by so much bad law) would be regenerated. Second, people's moral senses would be sharpened by their increased individual responsibility to preserve our freedoms. We would become, once again, a vigilant people, more keenly aware of the abuse of government power, jealous of our liberties, sensitive to the moral and philosophical prerequisites of freedom.

America's founders did not place their trust in a "professionalized" judiciary, controlled by lawyers, judges, and organized interests that make their living from government. They had a deep and abiding faith in the people themselves, and placed the ultimate power of the courtroom in the citizens' hands. Isn't it time that we returned to this fundamental principle of our republic? □

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THE UNSEEN COSTS OF FAMILY LEAVE

by Robert A. Sirico, CSP

Young women interviewing for jobs in the past year may have noticed potential employers looking carefully at their ring fingers. No, it's not an example of sexual harassment. Rather, employers are growing more skeptical of hiring (and promoting) young married women of child-bearing age.

Employers have long taken sex into account when hiring workers. The turnover rate for women is higher than for men, since a woman is more likely to leave her job to have a baby, or move when her spouse is transferred. Thus, companies were already less likely to hire and promote women.

But the Family and Medical Leave Act, which went into effect in July 1993, has *increased* the costs of hiring women. The law requires companies with more than 50 employees to grant full-time workers employed for one year 12 weeks of unpaid leave in any 12-month period. Employees can take this leave for birth or adoption of a child, or serious personal or family illness. And companies are legally bound to give workers their jobs back—or an equivalent position—when they return. Employers know that women of child-bearing age are most likely to take advantage of this government-mandated benefit. Thus, the "benefit" is another reason for firms to choose another candidate for a job.

Consider what Tama Starr, president of the ArtKraft Strauss company, told *The New York Times*: "If you are an employer, you will look at a young woman and say, 'Can we really entrust her to do crucial responsibilities that no one else can do because she's going to take three months off?'" Starr's answer to the economically logical, if politically incorrect, question: "You protect women so they can nurture babies and that's very nice, but you keep them at the lower end of the pay scale." Put bluntly, it is a lot easier to find temporary help to replace a clerical worker than a professional.

Some women have already felt the negative effects of the legislation. A spokesman for "Nine to Five," the National Association of Working Women, complained that their Long Island branch recently received 22 phone calls from pregnant women who believed they had been fired by employers seeking to get them out of the way before the law took effect. Sex discrimination is illegal, of course, but it is not always irrational. Employers are usually going to follow market dictates, since that's why they are in business. To root out rational sex discrimination would require the government to police virtually every employment decision in the country.

Obviously, for fear of lawsuits if nothing else, companies cannot simply stop hiring women. But business can try to hire women who seem least likely to take advantage of the new law. These days, an acknowledged

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lesbian would be a better bet than a blushing new bride. Similarly, a single woman over 35 is a more attractive candidate for a job or promotion since statistically she is less likely to marry and have children than her younger counterparts.

Thus, pro-family groups should have led the fight against family-leave legislation. Unfortunately, however, many believed the liberals' claim that family leave really was good for the family. Isn't it "pro-family" for employers to give women 12 weeks off to have kids? Not when the government mandates it, creating a powerful incentive for women with professional aspirations to remain not only childless but also single.

Government intervention in the name of the family didn't begin with this legislation and, unfortunately, won't end with it. The next step, demanded by many family-leave advocates, will be to require companies to give employees paid leave—something that would dramatically increase the disincentive to hiring women. And if the inconvenience of children is keeping women from being company workers, politicians are likely to push for increased subsidies for and regulation of day care, if not federally run centers.

Moreover, the Family and Medical Leave Act must be considered in the context of other laws that restrict the labor market. Labor Secretary Robert Reich, for example, wants to raise the minimum wage and index it to the rate of inflation. If an employer can't afford to pay up, he will have to let workers go. And if Congress passes the administration's health-care plan, businesses will have additional heavy expenses to bear.

Poor economic conditions, largely resulting from misguided federal fiscal and monetary policies, in conjunction with ever-higher rates of taxation, have forced many mothers to work even when they would prefer to remain home with their children. The government's first priority, then, should be to help relieve the financial pressure on women to work. At the same time, it should drop measures that artificially inflate the costs of hiring mothers. Officials should allow women to negotiate their own contracts, making the choice of salary levels and benefits that best meet their own needs and that of their families.

Many politicians have paid lip service to reversing the breakdown of the family. Federally mandated family leave was one of their answers. But the family is a natural product of a free society and needs no special privileges from government to thrive. American families would be better off if government undid the damage it has previously caused, instead of "helping" by passing ever more counterproductive measures like family leave. □

Personal Freedom and Individual Responsibility

IDEAS ON LIBERTY

Few of us seem to want to keep government out of our personal affairs and responsibilities. Many of us seem to favor various types of government-guaranteed and compulsory "security." We *say* that we want personal freedom, but we *demand* government housing, government price controls, government-guaranteed jobs and wages. We *boast* that we are responsible persons, but we *vote* for candidates who promise us special privileges, government pensions, and government subsidies.

Many of us are drifting back to that old concept of government that our forefathers feared and rejected. Many of us are now looking to government for security. Many of us are no longer willing to accept individual responsibility for our own welfare. Yet personal freedom cannot exist without individual responsibility.

—DEAN RUSSELL

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THE FREEMAN
IDEAS ON LIBERTY

SCHOOL VIOLENCE

by John Hood

When politicians talk about education issues, they often mention such topics as school spending, teacher quality, parental involvement, and the curriculum. But when *teachers* talk about education issues, they almost always zero in on the topic that most concerns them: school violence. In talking to teachers around my home state of North Carolina, I have found this to be universally true. Teachers bring it up—whether it's retelling a "horror story," complaining about school boards and lawyers protecting students from punishment, or simply observing that students "aren't what they used to be."

The public seems to share teachers' concerns about escalating violence in our schools. Remember the film *Lean on Me*? Despite carping from the education establishment—made up, to a large extent, of psychologists, consultants, professors of education, and professional activists—the film, which presented a story of one principal's tough stand against school violence, captured the imagination of movie audiences. A less successful but arguably better film, *Stand and Deliver*, dealt with the motivational and instructional techniques of Los Angeles math teacher Jaime Escalante, who used humor as well as "tough love" to teach calculus to a class of poor, sometimes violent teens. Other movies on gang life, teenage violence, and the drug subculture have also scored with audiences, while public opinion polls have found great concern about discipline and violence issues. Again, the public perception, at least, is that things "aren't what they used to be."

And the evidence is that they aren't. Violence in schools is up. Discipline is less predictable and not uniformly enforced. Students are, according to most teachers, more difficult to keep quiet, harder to teach, and deficient in basic personal and behavioral skills. Yet educational activists tend to focus more on opposing discipline practices they abhor—such as corporal punishment and expulsion—than on addressing the problem. In fact, today's public educators are probably incapable of dealing effectively with school violence and discipline problems. To do so requires rethinking how education is organized and the proper relationship between pupil and teacher, and more generally, between pupil and school.

Defining the Problem

No one keeps comprehensive statistics about school violence, but the numbers we do have are distressing, to say the least. Young people, who represent about 20 percent of the population, account for over 40 percent of reported crimes—and almost half of the youths charged with serious offenses are under 15. Some researchers suggest that the level of violent crime perpetrated by juveniles is three times greater today than it was in 1960. Many of these acts are

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committed at school, some with guns or other dangerous weapons.

A 1987 survey by the U.S. Department of Health and Human Services found that more than a third of eighth and tenth graders said they had been threatened with some sort of violence while at school. Fourteen percent reported being robbed and 13 percent said they had been attacked within the past year. Another report, by the National School Safety Center, found that:

- Almost 300,000 students are attacked in schools every month.
- Over 2 million students are the victims of theft.
- Approximately 5,200 secondary school teachers are physically attacked at school in a month's time, while 6,000 per month report extortion or robberies against them.

A few states have generated more recent numbers. A 1992 survey by North Carolina's Task Force on School Violence found that 59 percent of school systems reported an increase in violent behavior over the previous five years. School superintendents also reported marked increases in the prevalence of guns, knives, and other weapons at school. During this same time period, the number of reported arrests of young people 15 years old or younger for violent offenses doubled.

While these crime and violence numbers are shocking, by far the most pervasive problem is not *criminal* behavior per se, but a destructive and painful pattern of misbehavior, threats, and disrespect directed toward teachers and principals. This problem is harder to quantify, because no crime report is generated, but teachers have noticed a change in student behavior over the last 30 years or so. *Instructor* magazine columnist Adele M. Brodkin began to call attention to the problem with a series of interview features in 1990. Brodkin asked Wendy Jacobs, a fifth- and sixth-grade teacher in Caswell County, North Carolina, what teachers find most challenging about teaching today's children. "That's easy," Jacobs replied, "the biggest challenge is dealing with discipline. We have to contend with disruptive behavior, fighting amongst the kids, shouting, physical and verbal abuse, acting silly, being disrespectful of the teacher—all sort of behavior that can take so much of a teacher's time and energy."

William C. Lane, Jr., an assistant principal at Dunbar Middle School in Ft. Myers, Florida, says that the process of gaining control over the classroom is in fact "the cornerstone" of education and "an integral part of an effective school." Older teachers who remember a time of stronger discipline and fewer problems with students are especially vocal about the change in their perception of child behavior. A July 1989 survey by the American Federation of Teachers reported that over 80 percent of AFT officials around the country considered teenage violence a bigger problem today than in the past. Charles H. Wolfgang, a professor of early childhood education at Florida State University, tells of meeting a former English teacher of his at a neighborhood mall and proudly announcing that he, too, had become a teacher. "The twinkle I recalled as being ever-present in her warm blue eyes seemed to be missing," Wolfgang remembers. "As I spoke to her of our shared profession, her body stiffened and she responded in a cold tone of voice. 'I retired last year, thank God! I am glad to have gotten out of teaching. Students have changed. They certainly aren't interested in learning! And there are just too many discipline problems.'"

In fact, surveys for *Phi Delta Kappan* (a prominent education magazine) by the Gallup Organization have consistently ranked violence and discipline problems as one of the major reasons why public-school teachers leave the profession—a finding buttressed by the fact that private schools, which generally pay lower salaries and offer fewer benefits to their teaching staff, often receive plenty of applications from public-school teachers. The flight of good teachers from public schools can't be explained only by increasing safety concerns, but violence is undoubtedly an important factor in many cases. In *Policy Review*, Ben Wildavsky reported the case of Tom Masty,

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a teacher at a South Florida middle school. In Masty's first 10 weeks at the school, he wrote over 300 referrals for student misconduct. He confiscated weapons, broke up fights, and struggled to maintain control over his classroom. He quit shortly afterward.

Why Violence Is Increasing

Obviously, the wave of American school violence in many ways reflects underlying social trends. Crime generally has increased over the last several decades as well, so it's not surprising that violent and criminal behavior has risen in schools.

An important explanation of the rise in school violence can be found in changes in the American family. As the traditional two-parent model has given way to escalating numbers of single-parent families, children have often been put at risk, neglected, abused, and marginalized, resulting in discipline problems at school. One study of children with teenaged mothers found they were more likely to exhibit behavioral problems such as running away, fighting, stealing, and smoking than were children of older mothers. A 1989 study of children whose parents have divorced noted that five years after their parents broke up, only 34 percent of the children were clearly doing well at school. The remainder exhibited significant behavioral and academic problems. Many school administrators report that the majority of students suspended or expelled in their schools have either been sexually or physically abused or have a high incidence of substance abuse in the family.

While many of these social trends are partially or completely out of the reach of public policy, some government activities—such as the welfare system and punitive taxation of families—put pressure on families. Researchers such as Charles Murray and Mickey Kaus have identified at least some link between federal welfare payments and undesirable behavior. By subsidizing broken families, welfare can rob children of the stable home life they need to develop into healthy, well-adjusted teens.

But blaming the entire problem of school violence on social trends and family breakup would be a mistake, since it would ignore the crucial role of the school in setting rules of behavior and enforcing them. School policies do affect student behavior, as the experience of inner-city Catholic schools and other private schools demonstrates. Not surprisingly, students respond to credible promises of punishment and come to respect authority when it is exercised constantly and uniformly.

Unfortunately, the modern public school in America is ill-suited to develop a realistic response to school violence. A host of administrative decisions, court rulings, and legislative actions have created such a maze of regulations that school principals and teachers are often unable to exercise meaningful control over their schools. Furthermore, the prevailing "ethos" in the education establishment—made up of researchers, administrators, and bureaucrats—is suspicious of many forms of punishment, and exhibits a fixation with "sensitivity training" and building self-esteem among students.

Legal Restrictions and School Discipline

A range of school disciplinary measures, ranging from public embarrassment to expulsion, have been successfully challenged in court. In the 1975 case *Goss* v. *Lopez*, the U.S. Supreme Court decided that the due process clause of the Fourteenth Amendment gave students the right to receive oral or written notice of the charges against them and, if they deny the charges, an explanation of the evidence and a chance to tell their side of the story. While no formal hearing was required for short-term suspensions, the Court suggested that more formal procedures might be required to impose longer suspensions or expulsions. While suspension remains an important response to acts of violence by students, these procedural limitations have made administrators more hesitant to use them.

Restrictions on suspension and expulsion

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are especially troubling because of the great damage that violent and disruptive students can do to the educational process. These students not only disrupt the classroom, thus making it difficult for other students to learn, but also generally weaken the authority of teachers and administrators. "This type of student," writes education researcher Kurran Heston, "has a negative effect on everyone around him or her." It's in the interest of the majority of students that schools be able to quickly eject such students from class. "Eighty to ninety percent of the kids in a classroom are good kids," Oakland, California, schoolteacher Ruth Meltsner told *Policy Review*. "A small number are impossible and you spend all your time dealing with them."

Other decisions have further limited school disciplinary practices. Indeed, Heston notes that since 1950, "schools have been placed under the jurisdiction of the courts, whereas the court may decide it is necessary to step in regarding discipline." James S. Coleman, who has conducted landmark studies comparing public and private school students, argues that "the growth of student rights constitutes a fundamental change in the relation of the school to the student, which had been that of trustee for parental authority." This has been replaced, Coleman says, by a relation in which the student "is regarded as having full civil rights."

Extending civil-rights protection to unruly students has created an unworkable, and sometimes absurd, situation in public schools. "The due process system assumes bad faith on the part of teachers," says Bruce A. Miller, special counsel to the American Federation of Teachers, "but teachers aren't lawyers—they have to have some freedom of action." Sociologist Jackson Toby agrees, and observed that a generation ago it was possible for principals to rule schools autocratically, to suspend or expel students without much regard for procedure. While some injustices occurred, the administrators were able to avoid significant violence and discipline problems. "Student assaults on teachers were punished so swiftly that they were almost unthinkable," Toby wrote.

But it is not only the most stringent disciplinary actions that are subject to judicial negation. Consider, for example, the commonsensical idea that teachers and principals should be able to reduce student grades as a punishment for constant misconduct or violence. Several courts have struck down grade-reduction policies, treating grades earned for academic performance as a constitutionally protected "property interest."

Applying the Criminal Justice Model to Schools

A number of other actions—ranging from locker searches to dress codes—are frequently challenged by students, parents, politicians, and judges. Applying the criminal justice model to the school situation reflects a strange sense of priorities. Fascinated with whether or not an administrator has "probable cause" to search a locker—which is, after all, the property of the school and not the student—these critics prevent administrators from controlling the availability of weapons and drugs on school grounds. (Of course, administrators have at times gone too far—initiating strip searches without reasonable cause, for instance. Thus, schools must remain ultimately accountable for their decisions.)

Even a modest policy such as a dress code can help reduce discipline problems and even violence at school. So-called "gang" clothing often sparks conflict between students, while valuable jewelry or athletic shoes become the objectives in robberies and thefts. Such restrictions are obviously unthinkable in adult society, but the school environment is—or, at least, should be—different.

Not only are school policies found to violate students' so-called constitutional rights, but school officials are also potentially liable for civil damages. Naturally, administrators act increasingly warily when disciplining students. Classroom safety and student performance have deteriorated as a result.

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How the Education Establishment Views Discipline

Surveying the academic literature on school violence and discipline will leave the average person with an almost irresistible urge to alternately laugh and cry. When you see such article titles as "Should Students Be Punished?" and "Multicultural Classroom Management," you know you've entered a world of make-believe, divorced from the reality of dangerous classrooms and disruptive students. "The case against punishment has been steadily growing," wrote John Martin Rich, a professor of education at the University of Texas at Austin. "Critics claim that [even] nonphysical punishment can damage relationships, create resentment, and compel rather than encourage obedience. Moreover, punishment may promote school absenteeism, dropping out, school vandalism, and excessive anxiety." Education "experts" hated the film *Lean on Me* because they thought it sent an overly simplistic message about the efficacy of discipline and expulsion to reduce violence and increase student achievement. "Its popularity shows how badly the public can be deceived when offered easy solutions to its fears of teenagers, blacks, Hispanics, drugs, and crime," wrote one particularly excitable professor in *Education Week*. "In fact, the public support [Joe] Clark has gained for his tough-guy antics may well demonstrate the fragility of democracy."

The self-esteem craze is particularly amusing. Over the past couple of decades, programs to boost self-esteem among students have proliferated in many school systems. "The litany of statistics about self-destructive tendencies such as substance abuse, crime, and suicide must surely be seen as a signal from young people that many do not find much about themselves to like," wrote education professor James A. Beane in *Educational Leadership*, a prominent journal. Beane argues that enhancing self-esteem in school will, in addition to addressing behavioral and academic problems, "extend the idea of personal development beyond coping with problems and into personal efficacy or power, which, in turn, may lead toward action," thereby helping to "build the personal and collective efficacy that helps us out of the morass of inequity that plagues us."

Beane and others assume that a lack of self-esteem leads to crime and substance abuse. In fact, violent students are often fixated with themselves and quite comfortable with their actions—*and continue to commit crimes because they think they won't be punished.*

Other education "experts" contend that school violence stems from racial and cultural inequities and therefore cannot be effectively combatted by disciplinary efforts. Herbert Grossman, a teacher at San Jose State University, wrote in *Contemporary Education* that the population of the United States is rapidly becoming less "EuroAmerican." As a result, he says, fewer students respond positively to and profit from classroom management techniques "that have been designed with EuroAmerican middle-class students in mind." Grossman advocates "cultural sensitivity" when operating classrooms containing racial minorities. What about misbehavior and discipline? Grossman questions whether minority students can be expected to "sit in a quiet and controlled manner."

Education "experts" often argue that discipline is used in a discriminatory manner, and that attempts to combat school violence are merely smokescreens for punitive actions against minority students. Prejudice, Grossman writes, "drives many minority and working-class students to actively resist both their teachers and the system by purposefully misbehaving." Prejudice, he continues, "may also contribute to the unnecessary suspension of so many African-American, Hispanic, and working-class students." In conclusion, Grossman asserts that "the elimination of teacher prejudice is one of the most important steps educators can take to reduce disciplinary problems with minority students."

Both the self-esteem and multicultural fixations represent a fundamental challenge

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to the role of punishment and discipline in deterring school violence. Even more radical theorists enjoy some following in the education establishment, which has traditionally included radicals whose view of incorrigible students and nonconformists was more positive than negative. They're the kind of people who refer to the 1992 riots in Los Angeles as a "rebellion." In the school context, they view strong action against violent students as punishing society's victims, rather than addressing crime's so-called "root causes."

Toward Solutions

Radical theorists like these would present little threat to sound school administration if it were not for the current structure of American education. A system of publicly owned, controlled, and regulated schools, staffed by public employees and subject to the control of outside public authorities, is incapable of withstanding today's assault against punishment and common sense. Similarly, the legal restraints and requirements that have been placed on the administration of school discipline and security measures exist because of school's public nature.

In some districts, to be sure, violence has become so common that traditional obstacles to security measures have been overcome. A number of schools have banned gang clothing and insignia, as well as opaque book bags. San Diego's school system got rid of lockers, which resulted in inconvenience for students but also reduced gun crimes, robberies, and graffiti. Programs to encourage positive behavior and involve parents are great, says San Diego school police chief Alex Rascon, but in the meantime "the answer is to lock the campuses down. Have everyone enter through one door, sign in, and have permission to see a teacher ahead of time." Good security, Rascon adds, is inconvenient "but we just cannot dilly-dally around with the way things are now." It's unfortunate, however, that conditions have to escalate to crisis level before school administrators are given leave to take basic steps to reduce the threat of violence.

Private schools, by comparison, often maintain strict and uniform regulations that result in few incidents of violence or disruption, even in inner cities or other areas where crime is an integral part of the surrounding neighborhood. Private schools mete out not only more effective, but in many students' minds, fairer discipline, according to James Coleman: "This suggests that the legalistic approach to ensuring fairness in discipline may be less effective than other approaches . . . [and] may indeed be counterproductive for effectiveness of discipline."

In a private school setting, the role of the student is not that of "citizen" (to use the Supreme Court's term) with constitutional rights. Rather, the relationship with teacher and administrator is an economic one; if school personnel no longer believe they can handle a violent student, they do not have to continue providing him with educational services. In addition, private schools are often smaller, less bureaucratic, and, frankly, better able to keep kids interested in learning—all of which contribute to a greater sense of safety and security.

Thus, to address the epidemic of school violence in America, we will have to reconsider the governance of schools themselves. Any other measure—from peer counseling to handgun control—will ultimately fail without a fundamental change in the relationship between student and school. Schools must discipline, but they will be free to do so only when released from the political constraints of the present system. At the same time, they must be held directly accountable to parents and students (their customers) if punishment becomes capricious or excessive. In short, we must adopt a private model for education. The intellectual and psychological development of all our children—and, some cases, their lives—depend on it. □

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THE NEW YORK ASBESTOS DEBACLE

by Tim Brown

In August 6th of last year a bomb went off, sending shockwaves throughout the New York City public school system. The explosion, which subjected millions of parents and schoolchildren to fear, anxiety, and emotional distress, was not set by terrorists, but by politicians. It was the result of a national climate of environmental hysteria and an urban political system that could not rationally deal with three words—possible asbestos contamination.

The day before, special investigators from the City's School Construction Authority Inspector General's office called the State Department of Education in Albany to ask if they could see the asbestos management plans for each of the 1,069 New York City public schools. Without warning, investigators showed up 20 minutes later armed with service revolvers and search warrants. What they found, as they pored over thousands of documents, was that the school reports: "in addition to being incomplete and inaccurate, are so confusing and poorly organized that even an expert would have difficulty in determining specifically where asbestos is present in a particular school. For the ordinary concerned parent or teacher, the reports are incomprehensible."

The next day New York Mayor David Dinkins held a press conference and ordered every New York City public school closed pending a reinspection for asbestos contamination. Operation Clean House had begun.

The New York asbestos saga really began in 1986 with the passage of the Asbestos Hazard Emergency Response Act (AHERA) which mandated that local governments survey all schools to inventory and identify asbestos-containing material. New York's original inspection process began in 1988 and was conducted by a 53-member Asbestos Task Force, under the School Construction Authority. The inspections were originally to be completed in October 1988, but the task force asked for an extension until May 1989. As of February 1989, only 630 inspections had been completed; at least 300 inspection reports were filed within the last few days of the deadline. Task force inspectors allegedly fabricated reports to indicate that inspections had taken place when in fact they had not.

By 1990 construction workers and building inspectors were reporting the discovery of damaged, exposed asbestos during school renovations in places that had been declared free of asbestos. Only in 1993 was the Inspector General's office asked to investigate, however, after which city officials panicked.

Then they mismanaged the ensuing public communications effort. In fact, the actual risk of asbestos exposure to children was extremely low. The city's acting Health Commissioner, Dr. Benjamin Chu, said that there was no evidence that students and staff

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had been exposed or harmed, and there "is really no basis for alarm now." Even the Inspector General's report that set the stage for Operation Clean House admitted that "Although the AHERA reports may be completely unreliable, it does not necessarily follow that every school is unsafe or must be closed." But the mayor's precipitous school closings left parents convinced that their children had been at risk. And the government would not release any specific information on which schools had been found to contain damaged asbestos, until after the particular school had been cleaned up, further reducing the city's credibility: John C. Fager, co-chairman of the Parents Coalition for Education, said that "Parents are totally in the dark . . . not informing them is just inviting more fear and hysteria."

However, city officials, too, were obviously in the dark. Contrary to popular assumptions, neither AHERA, nor Environmental Protection Agency regulations, nor state environmental laws required closure of all the schools. After all, the schools remained open during the original AHERA inspections. Rather, like so many environmental issues, asbestos in schools is a political rather than scientific issue.

Mugged by Reality

But even the politicians eventually had to give in to reality. With only a handful of trained and certified asbestos inspectors, their original Herculean goal of visiting 35 schools a day was never realistic. As the deadline neared, and the pressure to open the schools on time increased, inspectors faced the same deadline pressures as the first asbestos task force. With 18 days to go only 197 schools had been inspected, leaving 743 to go. Something had to give. The new Schools Chancellor, Ramon C. Cortines, declared that all schools would open on September 20 except for a handful in which asbestos would be sealed or removed. As Cortines admitted, "If we had known what we know now on the 9th of September we might have made a decision to open [the schools on time]."

Obviously, the actual risk posed by asbestos did not change throughout this process, but rather, remained somewhere between hundreds and thousands of times lower that other everyday hazards facing schoolchildren. Scientists agree that the mere presence of asbestos does not pose a hazard if the asbestos is encapsulated—in wall plaster, for instance. Only if asbestos is damaged so that the fibers are exposed to the air is a person likely to inhale asbestos particles, and even then, a very large concentration of airborne asbestos is necessary to pose a health risk. Yet, the city never attempted to measure airborne asbestos contamination, the only empirical evidence upon which to base a decision. In mid-September, a group of 17 scientists criticized city officials for not taking into account the wealth of scientific data available on asbestos.

As it turns out, samples taken after the school closings revealed particle levels below the Occupational Safety and Health Administration standards, much lower than safe limits, and *even lower than ambient outside levels*. The latter should come as no surprise. A $4 million EPA review of asbestos data, including a survey of 170 schools published in 1991 by the Health Effects Institute-Asbestos Research, found indoor asbestos levels to be lower than that outside buildings.

Unfortunately, the asbestos scare reflects a larger pattern: the routine politicization of the environment in areas ranging from Alar to global warming. Off the record, even New York city officials admitted that closing the schools was less a scientific necessity and more a political remedy to mollify irate parents who had lost confidence in the school system.

In the end, the schools reopened. Along the way asbestos contractors made some money, parents were frightened, politicians postured, and scientists struggled to be heard. But while the New York schools seemed to get back to normal, the public remains as vulnerable as ever to new attacks of environmental hysteria—perhaps involving lead poisoning, perhaps ozone depletion, or perhaps something else. □

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BOOKS

The Rise and Fall of Leftist Radicalism in America

by Edward Walter

Praeger Publishers, Westport, Connecticut
1992 • 194 pages • $45.00

Reviewed by David Osterfeld

Edward Walter's *The Rise and Fall of Leftist Radicalism in America* is, in the author's words, "a defense of liberal democracy and the United States as its foremost practitioner" from the onslaught of the leftist radicals, whose attacks he views as "devious, unfair, and unprincipled."

What united the numerous strains of leftist radicals, says Walter, is not their vision of an alternative society but their uncompromising opposition to free market capitalism and, consequently, the United States. The primary reason that intellectuals, serious artists and writers as well as many in academe, harbor such resentment against American society, the author claims, is that, in contrast to, say, Europe where intellectuals are at least respected if not handsomely compensated, they see themselves as being neglected and even derided by the American mass media which, in its quest for profit, panders to the lowest common denominator. The irony is that while the anti-American mindset of some intellectuals stems from their feeling of being unjustly ignored, they actually have a significant, long-run impact on American attitudes and beliefs emanating from their strategic position as educators.

It is mainly for this reason, believes Walter, that a stable, prosperous, and open nation such as the United States finds itself beset with chronic, fundamental, and general opposition.

What most disturbs the author is the radical leftists' unscrupulous, even Machiavellian, tactics, which Walter does a superb job of documenting. As Walter puts it, a moral principle "was hired like a cab to get the radical leftists to the destination they desired . . . and dismissed . . . when it would take them elsewhere. The destination was all that mattered." The radical leftists hated America because it was capitalist, and thus intrinsically immoral; they embraced the Soviet Union since it was "anti-capitalist and anti-American" and therefore morally sacrosanct. The task was to defend the Soviet Union by adopting whatever "moral principles" the situation called for.

Walter examines the abuse of such terms as "liberty" and "democracy" running throughout radical leftist literature. Massive violations of civil liberties in the Soviet Union were rationalized by American leftists such as Roger Baldwin, founder of the American Civil Liberties Union, who claimed that there were two kinds of liberty, economic and civil. The latter was more important than the former and since some violations of the former were necessary to achieve the latter, they were justified. America, by contrast, was a system based on the economic serfdom of capitalism.

And Yale sociologist Jerome Davis contended that although America may have political democracy, that was of little consequence since it did nothing to prevent "industrial autocracy." By contrast, although the Soviet Union was "politically dictatorial," that was unimportant in light of its democratic economic institutions. By such sophistries, Walter shows, radical leftists were able to posture as champions of liberty and democracy while simultaneously justifying political tyranny.

Walter appropriately describes the radical left's track record as "shameful." Stalin's liquidation of millions of kulaks, or middle-class farmers, because they resisted agricultural collectivization was justified as necessary in order to eliminate the reactionary elements blocking the transition to Communism. A good end, pronounced Walter Durranty, Moscow correspondent for the *New York Times*, "justifies any means however cruel." The treatment of tens of thousands who were executed or imprisoned during the

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Soviet show-trials of the 1930s was defended on the ground that the accused had not proven their innocence, thereby endorsing the legal principle that one is guilty until proven innocent. Moreover, radical leftists argued in a moral asymmetry of breathtaking proportions, Americans had no right to take the Soviets to task since the convictions of Sacco and Vanzetti in the 1920s showed that the United States was just as bad. And besides, said writers like Corliss Lamont, Soviet oppression was made necessary by the imperialist threat of Western capitalism, thereby placing responsibility for Soviet police state tactics in American hands and conveniently exonerating the Soviet Union.

Yet, radical leftists repudiated these propositions when it suited them. During the McCarthy period in the early 1950s, radical leftists like Lamont defended the First Amendment rights of free speech and press on the ground that they were categorical guarantees, repudiating their earlier utilitarian position that an important end justifies the abridgment of rights. Congressional loyalty investigations were condemned because they violated the traditional presumption that individuals "are not guilty until evidence proves their guilt." And the traditional American legal system, guaranteeing rights for the accused, was suddenly seen as not so bad after all.

Walter convincingly demonstrates that both the abuse of language and the misuse of ethical principles have been hallmarks of leftist radicalism down to the present. Although far from commendable, the record of the South Vietnamese governments during the Vietnam war was far superior to the record of either the government of North Vietnam during the war or the government that replaced it following the war. And while hardly admirable, the record of the Shah of Iran, by any reasonable reckoning, was much better than that of the Ayatollah. Yet, in both cases, it was the former that was vilified and excoriated by the radicals while the latter was applauded and given every benefit of the doubt until there was no doubt left, at which time leftists turned their attention to other matters, such as El Salvador. The only explanation for such behavior, believes Walter, is the radical left's hatred for capitalism and their desire to weaken U.S. foreign policy.

Walter is far from a mere cheerleader for America. He readily acknowledges that the United States made mistakes and at times these were serious. Vietnam is a case in point, and he is certainly no fan of McCarthy. But since policies are made by human beings and human beings are fallible, mistakes are to be expected in every society. What Walter stresses, however, is both the self-corrective character of liberal democracy, where wrongs can be peacefully corrected and the victims recompensed, and the fact that *only* societies in which free markets have flourished and natural rights have been respected have succeeded in improving the material positions of all its members.

The Rise and Fall of Leftist Radicalism in America provides the reader with engaging reinterpretations of the major events in twentieth-century America. Walter's interpretations are compelling largely because, in contrast to the Machiavellian tactics of the leftist radicals documented in his book, his key terms are so carefully defined and consistently applied. □

The late David Osterfeld was a professor of political science at St. Joseph's College in Rensselaer, Indiana.

A Retrospective on the Bretton Woods System—Lessons for International Monetary Reform

edited by Michael D. Bordo and Barry Eichengreen

The University of Chicago Press • 1993
690 pages • $75.00

Reviewed by Robert Batemarco

What constitutes the ideal international monetary system? To this reviewer, and presumably most readers of *The Free-*

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man, it would be a system which could not be manipulated by governments and central bankers, thus subject to neither inflationary expansions nor deflationary collapses. Its various currencies would all be fully convertible into a base money that would be free of exchange rate risks which might impede the free flow of goods and capital between nations. Indeed, under the ideal system, exchange between people in different nations would be no more complicated than trade between people in different states.

A Retrospective on the Bretton Woods System makes obvious just how far we are from achieving this ideal and showcases many of the attitudes responsible for our current problems. The volume consists of twelve papers plus two panel discussions at a conference held under the auspices of the National Bureau of Economic Research on the twentieth anniversary of the breakdown of the Bretton Woods par value system.

The standard interpretation of the international monetary system parallels the standard interpretation of Keynesian economics, which, as this volume often reminds us, inspired Bretton Woods. Just as Keynesianism was thought to have "saved" capitalism by removing the balanced-budget constraint which had prevented governments from dealing with the otherwise intractable problem of the business cycle, so the Bretton Woods system was seen as "restoring" the liberal international trading system by uncoupling international and domestic policymaking. The rapid pace of growth of global output and trade in the post-war period through 1973 is usually trotted out as evidence to this effect, although several contributors at least consider the possibility that the Bretton Woods system was not responsible for that performance. In fact, the shortcomings of both Bretton Woods and the system's underlying Keynesian theories prevented either from lasting a whole generation. A large part of *A Retrospective* discusses the factors which led to the system's demise.

The book is divided into three main sections, dealing with Bretton Woods's origins, operations, and legacy, plus a conclusion. The initial article, written by editor Michael Bordo, traces the evolution of the Bretton Woods system from its initial arrangements through its inglorious replacement by floating exchange rates in 1973. Bordo weaves a wealth of historical and statistical detail into a coherent narrative. He also compares the macroeconomic performance of the system with the classical gold standard, the interwar gold exchange standard which degenerated into a free-for-all of floating rates, and the post-Bretton Woods set-up.

Bordo's characterization of Bretton Woods as exhibiting "the best overall macro performance of any regime," including the gold standard, rests on his judgment that price stability should be accorded lower priority than per capita growth of real GDP. It also leads him to find it paradoxical that the Bretton Woods system was so short-lived (the U.S. shut the gold window, effectively ending the par value system, only thirteen years after the European currencies achieved *de facto* convertibility).

He believes part of the solution to this paradox to be the occurrence of events—particularly the rapid recovery of Europe from the war and the subsequent replacement of a dollar shortage with a dollar glut—which the Bretton Woods planners could not foresee. He attributes the rest to either flaws in the system or inappropriate policies by member countries, especially the United States. He points, for example, to the built-in instability of any gold exchange standard plus the fact that capital mobility made it too costly for nations to adjust their exchange rates in the way permitted by the system. As inappropriate policies he cites America's inflationary course taken after 1965 and the failure of countries with a dollar surplus to adjust. I question this dichotomy between systemic flaws and bad policies: a system which metes out no effective penalty for bad policies is for that reason a flawed system. Maurice Obstfeld makes this same point in his paper, noting that "a well-designed system should provide incentives that ensure successful operation." Bordo himself admits that Bretton Woods was, in

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some ways, a failure. Except for deflation, he writes, "the problems of the interwar system that Bretton Woods was designed to avoid re-emerged with a vengeance."

Despite providing some rather incisive analysis of the problems with Bretton Woods' attempt to devise a workable international monetary system, the book's authors are by and large enamored of fiat money and the right of nations to inflate their currencies at their own pace. Among the most egregious examples of this viewpoint are Bordo's and Obstfeld's citing as a problem the failure of countries with surplus dollars to adjust (i.e., to inflate as rapidly as their trading partners), Genberg's and Swoboda's calls for a world currency and central bank, and Garber's statement that "There need be no inherent problem with a fiat monetary system with one country's central bank providing the liquid funds."

The one common denominator of these views is that the international monetary system must never permit the slightest hint of deflation. Thus, any kind of true gold standard, in which gold actually circulates as money and constitutes reserves into which all other forms of money are convertible, is anathema to the volume's contributors. Keynes himself described the system put in place at Bretton Woods as "the exact opposite of [a gold standard]." The aversion to gold might be defensible if the uninterrupted inflation which has characterized the last sixty years (with gold demonetized for the last twenty) had freed us from the business cycle. The record, however, clearly shows that the business cycle has continued, with neither gold nor deflation anywhere in sight to shoulder the blame.

Ultimately, the international monetary system set up at Bretton Woods was an attempt to shield nations from the consequences of irresponsible fiscal and monetary policies, in sharp contrast to the pre-war gold standard, which penalized such behavior. Bretton Woods did this by using exchange rate devaluations in an attempt to short-circuit the mechanism that normally triggers the slumps that follow inflationary booms. To the extent that governments and central banks *believed* that such a strategy would succeed, they were encouraged to engage in more inflationary policies. But since the laws of economics prevent nations from escaping boom-induced slumps, countries ended up with more downturns as well.

The primary value of *A Retrospective* lies in laying out enough facts about the Bretton Woods system to permit readers to draw this conclusion. The book's greatest failing lies in the reluctance of its contributors to make the same judgment. Instead, they stubbornly adhere to the belief that the problem is not with politically managed currencies, but rather only with the particular framework of management which was developed at Bretton Woods. □

Robert Batemarco teaches economics at Marymount College in Tarrytown, New York.

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—GEORGE SANTAYANA (1863–1952)

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